# SOCIAL SECURITY MISCELLANEOUS AND TECHNICAL IMPROVEMENTS ACT OF 1982

## HEARING

BEFORE THE

SUBCOMMITTEE ON SOCIAL SECURITY

OF THE

COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES
NINETY-SEVENTH CONGRESS

SECOND SESSION

ON

## H.R. 7326

TO AMEND TITLE II OF THE SOCIAL SECURITY ACT TO MAKE MISCELLANEOUS AND TECHNICAL IMPROVEMENTS RELATING TO CASH MANAGEMENT, GENDER-BASED DISTINCTIONS, COVERAGE, AND OTHER MATTERS UNDER THE OLD-AGE, SURVIVORS, AND DISABILITY INSURANCE PROGRAM

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DECEMBER 6, 1982

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**Serial 97–88**

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# CONTENTS

Page

Press release of Tuesday, November 30, 1982, announcing hearing ........ 1
H.R. 7326, text ........ 3

## WITNESSES

Social Security Administration, Paul Simmons, Deputy Commissioner for Programs and Policy; Louis D. Enoff, Deputy to the Deputy Commissioner; Mary Ross, Legislative Reference Officer; and Lucia Swanson, Deputy Chief, Coverage Branch, Office of Legislative and Regulatory Policy ........ 58
Department of the Treasury:
  C. Warren Carter, Deputy Assistant Secretary for Federal Finance ........ 72
  Irving E. Faunce, Jr., Deputy Commissioner, Bureau of Government Financial Operations ........ 75

Hercules Inc., Eldin H. Glanz and Gary G. Quintiere ........ 110
National Senior Citizens Law Center, Eileen Sweeney ........ 84
National Small Business Association, Paul H. Jackson ........ 114

## SUBMISSIONS FOR THE RECORD

Campbell, Nancy Duff, joint statement for American Association of University Women, American Nurses Association, National Commission on Working Women, National Council of Catholic Women, National Council of Jewish Women, National Federation of Business and Professional Women's Clubs, Inc., National Women's Health Network, National Women's Law Center, Older Women's League, Universalist Women's Federation, Women's Equity Action League, and Women's Legal Defense Fund ........ 163
Chamber of Commerce of the United States of America, Hilton Davis, letter ........ 162
Pfizer, Inc., statement ........ 166
Seiberling, Hon. John F., a Representative in Congress from the State of Ohio, statement ........ 161
Westinghouse Electric Corp., A. W. Frisch, letter and attachment ........ 167

# SOCIAL SECURITY MISCELLANEOUS AND TECHNICAL IMPROVEMENTS ACT OF 1982

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MONDAY, DECEMBER 6, 1982

House of Representatives,
Committee on Ways and Means,
Subcommittee on Social Security,
*Washington, D.C.*

The subcommittee met at 2 p.m., pursuant to notice, in room 1100, Longworth House Office Building, Hon. J. J. Pickle (chairman of the subcommittee) presiding.

[The press release announcing the hearing and a copy of the bill, H.R. 7326, follow:]

[Press release of Tuesday, November 30, 1982]

### HON. J. J. PICKLE (D-TEXAS), CHAIRMAN, SUBCOMMITTEE ON SOCIAL SECURITY OF THE COMMITTEE ON WAYS AND MEANS, ANNOUNCES A HEARING ON H.R. 7326, THE SOCIAL SECURITY MISCELLANEOUS AND TECHNICAL IMPROVEMENTS ACT OF 1982

The Honorable J. J. Pickle (D-Texas), Chairman of the Subcommittee on Social Security of the Committee on Ways and Means, U.S. House of Representatives, announced today that the Subcommittee will hold a hearing on H.R. 7326, the Social Security Miscellaneous and Technical Improvements Act of 1982. The hearing will be held on Monday, December 6, 1982, in room 1100 of the Longworth House Office Building beginning at 2:00 p.m.

H.R. 7326 contains a series of amendments to Title II of the Social Security Act of a relatively minor and technical nature. These amendments have for the most part been introduced in previous years as part of technical amendment bills. The bill contains no social security financing amendments, and none of its provisions would significantly affect either benefit amounts or eligibility. Therefore, testimony from public witnesses will be received only on the provisions of the bill as introduced. Both the Commissioner of Social Security and representatives of the Department of the Treasury will be testifying on the provisions of the bill.

### DETAILS FOR SUBMISSION OF REQUESTS TO BE HEARD

Requests to be heard must be received by telephone to Harriett Lawler [telephone (202) 225-3627] by noon, Friday, December 3, 1982. The request should be followed by a formal written request addressed to John J. Salmon, Chief Counsel, Committee on Ways and Means, U.S. House of Representatives, room 1102 Longworth House Office Building, Washington, D.C. 20515.

In order to assure the most productive use of the limited amount of time available to question hearing witnesses, witnesses scheduled to appear before the Subcommittee are required to submit 75 copies of their prepared statements to the full Committee office, room 1102 Longworth House Office Building, at least 24 hours in advance of their scheduled appearances.

Each statement to be presented to the Subcommittee or any written statement submitted for the record must contain the following information:

1. The name, full address, and capacity in which the witness will appear (as well as a telephone number where he or his designated representative may be reached);
2. A list of any clients or persons, or any organization for whom the witness appears; and

3. A topical outline or summary of comments and recommendations in the full statement.

### WRITTEN STATEMENTS IN LIEU OF PERSONAL APPEARANCE

Persons submitting a written statement in lieu of a personal appearance should submit at least six (6) copies of their statement by the close of business December 17, 1982, to John J. Salmon, Chief Counsel, Committee on Ways and Means, U.S. House of Representatives, Washington, D.C. 20515. If those filing written statements for the record of the printed hearing wish to have their statements distributed to the press and the interested public, they may submit 50 additional copies for this purpose if provided to the Committee during the course of the public hearing.

97TH CONGRESS
2D SESSION

# H. R. 7326

To amend title II of the Social Security Act to make miscellaneous and technical improvements relating to cash management, gender-based distinctions, coverage, and other matters under the old-age, survivors, and disability insurance program.

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IN THE HOUSE OF REPRESENTATIVES

NOVEMBER 30, 1982

Mr. PICKLE introduced the following bill; which was referred to the Committee on Ways and Means

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# A BILL

To amend title II of the Social Security Act to make miscellaneous and technical improvements relating to cash management, gender-based distinctions, coverage, and other matters under the old-age, survivors, and disability insurance program.

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,*

### SHORT TITLE

SECTION 1. This Act may be cited as the "Social Security Miscellaneous and Technical Improvements Act of 1982".

## TABLE OF CONTENTS

SEC. 2. The contents of this Act are as follows:

### TABLE OF CONTENTS

Sec. 1. Short title.
Sec. 2. Table of contents.

TITLE I—CASH MANAGEMENT

Sec. 101. Accounting for certain unnegotiated checks for benefits under the social security program.
Sec. 102. Float periods.
Sec. 103. Investment of Trust Fund assets.
Sec. 104. Interest on late State deposits.

TITLE II—ELIMINATION OF GENDER-BASED DISTINCTIONS

Sec. 201. Divorced husbands.
Sec. 202. Remarriage of surviving spouse before age 60.
Sec. 203. Illegitimate children.
Sec. 204. Transitional insured status.
Sec. 205. Equalization of benefits under section 228.
Sec. 206. Father's insurance benefits.
Sec. 207. Effect of marriage on childhood disability beneficiary.
Sec. 208. Effect of marriage on other benefits of dependents or survivors.
Sec. 209. Treatment of self-employment income in community property States.
Sec. 210. Credit for certain military service.
Sec. 211. Conforming amendments.
Sec. 212. Effective date of title II.

TITLE III—COVERAGE

Sec. 301. Coverage of employees of foreign affiliates of American employers.
Sec. 302. Extension of coverage by international social security agreement.
Sec. 303. Foreign earned income exclusion from net self-employment income.
Sec. 304. Social security tax treatment of cash or deferred compensation arrangements.
Sec. 305. Treatment of pay after age 62 as wages.
Sec. 306. Payments under simplified employee pension plans excluded from wages for purposes of benefit computation.
Sec. 307. Effect of changes in names of State and local employee groups in Utah.

TITLE IV—MISCELLANEOUS AND TECHNICAL AMENDMENTS

Sec. 401. Technical and conforming amendments to maximum family benefit provisions.
Sec. 402. Application of social security program to Northern Mariana Islands.
Sec. 403. Simplification of trust fund reimbursement computation with respect to benefits attributable to noncontributory wage credits for military service.
Sec. 404. Reduction from 72 to 70 of age beyond which no delayed retirement credits can be earned.
Sec. 405. Relaxation of insured status requirements for certain workers previously entitled to a period of disability.
Sec. 406. Protection of benefits of illegitimate children of disabled beneficiaries.

Sec. 407. Continuation of benefits of disabled widow or widower who marries a retired or disabled worker.
Sec. 408. One-month retroactivity of widow's and widower's insurance benefits.
Sec. 409. Non-assignability of benefits.
Sec. 410. Requirement of previous United States residency for alien dependents and survivors living outside the United States.

# TITLE I—CASH MANAGEMENT

## ACCOUNTING FOR CERTAIN UNNEGOTIATED CHECKS FOR BENEFITS UNDER THE SOCIAL SECURITY PROGRAM

SEC. 101. (a) Section 201 of the Social Security Act is amended by adding at the end thereof the following new subsection:

"(m)(1) The Secretary of the Treasury shall implement procedures to permit the identification of each check issued for benefits under this title that has not been presented for payment by the close of the twelfth month following the month of its issuance.

"(2) The Secretary of the Treasury shall, on a monthly basis, credit each of the Trust Funds for the amount of all benefit checks drawn on such Trust Fund more than 12 months previously but not presented for payment and not previously credited to such Trust Fund.

"(3) If a benefit check is presented for payment to the Treasury and the amount thereof has been previously credited pursuant to paragraph (2) to one of the Trust Funds, the Secretary of the Treasury shall nevertheless pay such check, if otherwise proper, recharge such Trust Fund, and notify the Secretary of Health and Human Services.

"(4) A benefit check bearing a current date may be issued to an individual who did not negotiate the original benefit check and who surrenders such check for cancellation if the Secretary of the Treasury determines it is necessary to effect proper payment of benefits.".

(b) The amendment made by subsection (a) shall apply with respect to all checks for benefits under title II of the Social Security Act which are issued on or after the first day of the twenty-fourth month following the month in which this Act is enacted.

(c)(1) The Secretary of the Treasury, within 60 days after the end of the fiscal year in which this Act is enacted and within 60 days after the end of each of the four succeeding fiscal years, shall transfer from the general fund of the Treasury to the Federal Old-Age and Survivors Insurance Trust Fund and to the Federal Disability Insurance Trust Fund such sums as may be necessary to reimburse such Trust Funds in the total amount of all checks which he and the Secretary of Health and Human Services jointly determine to be unnegotiated benefit checks as of the preceding September 30. After any amounts authorized by this subsection have been transferred to a Trust Fund with respect to any benefit check, the provisions of paragraphs (3) and (4) of section 201(m) of the Social Security Act (as added by subsection (a) of this section) shall be applicable to such check.

(2) As used in paragraph (1), the term "unnegotiated benefit checks" means checks for benefits under title II of the Social Security Act which are issued prior to the twenty-fourth month following the month in which this Act is enacted, which remain unnegotiated after the twelfth month following the date on which they were issued, and with respect to which no transfers have previously been made in accordance with the first sentence of such paragraph.

### FLOAT PERIODS

SEC. 102. (a) The Secretary of Health and Human Services and the Secretary of the Treasury shall jointly undertake, as soon as possible after the date of the enactment of this Act, a thorough study with respect to the period of time (hereafter in this section referred to as the "float period") between the issuance of checks from the general fund of the Treasury in payment of monthly insurance benefits under title II of the Social Security Act and the transfer to the general fund from the Federal Old-Age and Survivors Insurance Trust Fund or the Federal Disability Insurance Trust Fund, as applicable, of the amounts necessary to compensate the general fund for the issuance of such checks. Each such Secretary shall consult the other regularly during the course of the study and shall, as appropriate, provide the other with such information and assistance as he may require.

(b) The study shall include—

(1) an investigation of the feasibility and desirability of maintaining the float periods which are allowed as of the date of the enactment of this section in the procedures governing the payment of monthly insurance benefits under title II of the Social Security Act, and of the general feasibility and desirability of making adjustments in such procedures with respect to float periods; and

(2) a separate investigation of the feasibility and desirability of providing, as a specific form of adjustment in such procedures with respect to float periods, for the transfer each day to the general fund of the Treasury from the Federal Old-Age and Survivors Insurance Trust Fund and the Federal Disability Insurance Trust Fund, as appropriate, of amounts equal to the amounts of the checks referred to in subsection (a) which are paid by the Federal Reserve Banks on such day.

(c) In conducting the study required by subsection (a), the Secretaries shall consult, as appropriate, the Director of the Office of Management and Budget, and the Director shall provide the Secretaries with such information and assistance as they may require. The Secretaries shall also solicit the views of other appropriate officials and organizations.

(d)(1) Not later than six months after the date of the enactment of this Act, the Secretaries shall submit to the President and the Congress a report of the findings of the investigation required by subsection (b)(1), and the Secretary of the Treasury shall by regulation make such adjustments in the procedures governing the payment of monthly insurance benefits under title II of the Social Security Act with respect to float periods (other than adjustments in the form described in subsection (b)(2)) as may have been found in such investigation to be necessary or appropriate.

(2) Not later than twelve months after the date of the enactment of this Act, the Secretaries shall submit to the President and the Congress a report of the findings of the separate investigation required by subsection (b)(2), together with their recommendations with respect thereto; and, to the extent necessary or appropriate to carry out such recommendations, the Secretary of the Treasury shall by regulation make adjustments in the procedures with respect to float periods in the form described in such subsection.

### INVESTMENT OF TRUST FUND ASSETS

SEC. 103. (a) Section 201(d) of the Social Security Act is amended by striking out "(1)" and "(2)" in the third sentence, and by striking out the fifth sentence and inserting in lieu thereof the following: "Any such obligations issued for purchase by the Trust Funds—

"(1) shall bear interest at a rate equal to the higher of (A) the average market yield (computed by the Managing Trustee on the basis of market quotations as of the end of the calendar month next preceding the date of such issue) on all marketable obligations of the United States then forming a part of the public debt which are due or callable within less than four years from the end of such calendar month, or (B) the average market yield (so computed) on all marketable obligations of the United States then forming a part of the public debt which are not due or callable until the expiration of four years or more from the end of such month, and

"(2) shall have maturities, fixed with due regard for the needs of the Trust Funds, which are less than four years in any case where the interest rate is determined under clause (1)(A) or which are four years or more in any case where such rate is determined under clause (1)(B);

except that (i) where the average market yield as computed under clause (1)(A) or (1)(B), whichever is applicable, is not a multiple of one-eighth of 1 percent, the rate of interest on such obligations shall be the multiple of one-eighth of 1 percent nearest such market yield, and (ii) nothing in this sentence shall prevent the issuance, for purchase by the Trust

Funds, of certificates of indebtedness which have maturities of less than one year and which (without regard to whether clause (1)(A) or clause (1)(B) would otherwise apply) bear interest at the rate determined under clause (1)(A).".

(b) Section 1817(c) of such Act is amended by striking out "(1)" and "(2)" in the third sentence, and by striking out the fifth sentence and inserting in lieu thereof the following: "Any such obligations issued for purchase by the Trust Fund—

"(1) shall bear interest at a rate equal to the higher of (A) the average market yield (computed by the Managing Trustee on the basis of market quotations as of the end of the calendar month next preceding the date of such issue) on all marketable obligations of the United States then forming a part of the public debt which are due or callable within less than four years from the end of such calendar month, or (B) the average market yield (so computed) on all marketable obligations of the United States then forming a part of the public debt which are not due or callable until the expiration of four years or more from the end of such month, and

"(2) shall have maturities, fixed with due regard for the needs of the Trust Fund, which are less than four years in any case where the interest rate is determined under clause (1)(A) or which are four years or more in any case where such rate is determined under clause (1)(B);

except that (i) where the average market yield as computed under clause (1)(A) or (1)(B), whichever is applicable, is not a multiple of one-eighth of 1 percent, the rate of interest on such obligations shall be the multiple of one-eighth of 1 percent nearest such market yield, and (ii) nothing in this sentence shall prevent the issuance, for purchase by the Trust Fund, of certificates of indebtedness which have maturities of less than one year and which (without regard to whether clause (1)(A) or clause (1)(B) would otherwise apply) bear interest at the rate determined under clause (1)(A).".

(c) Section 1841(c) of such Act is amended by striking out "(1)" and "(2)" in the third sentence, and by striking out the fifth sentence and inserting in lieu thereof the following: "Any such obligations issued for purchase by the Trust Fund—

"(1) shall bear interest at a rate equal to the higher of (A) the average market yield (computed by the Managing Trustee on the basis of market quotations as of the end of the calendar month next preceding the date of such issue) on all marketable obligations of the United States then forming a part of the public debt which are due or callable within less than four years from the end of such calendar month, or (B) the average market yield (so computed) on all marketable obligations of the United States then forming a part of the public debt which are not due or callable until the expiration of four years or more from the end of such month, and

"(2) shall have maturities, fixed with due regard for the needs of the Trust Fund, which are less than four years in any case where the interest rate is determined under clause (1)(A) or which are four years or more in any case where such rate is determined under clause (1)(B);

except that (i) where the average market yield as computed under clause (1)(A) or (1)(B), whichever is applicable, is not a multiple of one-eighth of 1 percent, the rate of interest on such obligations shall be the multiple of one-eighth of 1 percent nearest such market yield, and (ii) nothing in this sentence shall prevent the issuance, for purchase by the Trust Fund, of certificates of indebtedness which have maturities of less than one year and which (without regard to whether clause (1)(A) or clause (1)(B) would otherwise apply) bear interest at the rate determined under clause (1)(A).".

(d) The amendments made by this section shall apply with respect to obligations which are issued (for purchase by one or more of the Trust Funds) after the month in which this Act is enacted.

### INTEREST ON LATE STATE DEPOSITS

SEC. 104. (a) Section 218(j) of the Social Security Act is amended by striking out "the rate of 6 per centum per annum" and inserting in lieu thereof "the annual rate established under section 6621 of the Internal Revenue Code of 1954".

(b) The amendment made by subsection (a) shall apply with respect to payments due for wages paid after December 31, 1983.

## TITLE II—ELIMINATION OF GENDER-BASED DISTINCTIONS

### DIVORCED HUSBANDS

SEC. 201. (a)(1) Section 202(c)(1) of the Social Security Act is amended, in the matter preceding subparagraph (A), by inserting "and every divorced husband (as defined in section 216(d))" before "of an individual" and by inserting "or such divorced husband" after "if such husband".

(2) Section 202(c)(1) of such Act is further amended—

(A) by striking out "and" at the end of subparagraph (B);

(B) by redesignating subparagraph (C) as subparagraph (D), and by inserting after subparagraph (B) the following new subparagraph:

"(C) in the case of a divorced husband, is not married, and"; and

(C) by striking out the matter following subparagraph (D) (as so redesignated) and inserting in lieu thereof the following:

"shall be entitled to a husband's insurance benefit for each month, beginning with—

"(i) in the case of a husband or divorced husband (as so defined) of an individual who is entitled to an old-age insurance benefit, if such husband or divorced husband has attained age 65, the first month in which he meets the criteria specified in subparagraphs (A), (B), (C), and (D), or

"(ii) in the case of a husband or divorced husband (as so defined) of—

"(I) an individual entitled to old-age insurance benefits, if such husband or divorced husband has not attained age 65, or

"(II) an individual entitled to disability insurance benefits,

the first month throughout which he is such a husband or divorced husband and meets the criteria specified in subparagraphs (B), (C), and (D) (if in such month he meets the criterion specified in subparagraph (A)), whichever is earlier, and ending with the month preceding the month to which any of the following occurs:

"(E) he dies,

"(F) such individual dies,

"(G) in the case of a husband, they are divorced and either (i) he has not attained age 62, or (ii) he has attained age 62 but has not been married to such individual for a period of 10 years immediately before the divorce became effective,

"(H) in the case of a divorced husband, he marries a person other than such individual,

"(I) he becomes entitled to an old-age or disability insurance benefit based on a primary insurance amount which is equal to or exceeds one-half of the primary insurance amount of such individual, or

"(J) such individual is not entitled to disability insurance benefits and is not entitled to old-age insurance benefits.".

(3) Section 202(c)(3) of such Act is amended by inserting "(or, in the case of a divorced husband, his former wife)" before "for such month".

(4) Section 202(c) of such Act is further amended by adding after paragraph (3) the following new paragraph:

"(4) In the case of any divorced husband who marries—

"(A) an individual entitled to benefits under subsection (b), (e), (g), or (h) of this section, or

"(B) an individual who has attained the age of 18 and is entitled to benefits under subsection (d), by reason of paragraph (1)(B)(ii) thereof,

such divorced husband's entitlement to benefits under this subsection, notwithstanding the provisions of paragraph (1) (but subject to subsection (s)), shall not be terminated by reason of such marriage.".

(5) Section 202(c)(2)(A) of such Act is amended by inserting "(or divorced husband)" after "payable to such husband".

(6) Section 202(b)(3)(A) of such Act is amended by striking out "(f)" and inserting in lieu thereof "(c), (f),".

(7) Section 202(c)(1)(D) of such Act (as redesignated by paragraph (2) of this subsection) is amended by striking out "his wife" and inserting in lieu thereof "such individual".

(8) Section 202(d)(5)(A) of such Act is amended by inserting "(c)," after "(b),".

(b)(1) Section 202(f)(1) of such Act is amended, in the matter preceding subparagraph (A), by inserting "and every surviving divorced husband (as defined in section 216(d))" before "of an individual" and by inserting "or such surviving divorced husband" after "if such widower".

(2) Section 202(f)(1) of such Act is further amended by striking out "his deceased wife" in subparagraph (D) and in the matter following subparagraph (F) and inserting in lieu thereof "such deceased individual".

(3) Paragraphs (3), (4), (6), and (7) of section 202(f) of such Act are each amended by inserting "or surviving divorced husband" after "widower" wherever it appears.

(4) Paragraph (3) of section 202(f) of such Act is further amended by striking out "his deceased wife" in subparagraph (A) and inserting in lieu thereof "such deceased individual", and by striking out "wife" wherever it appears in subparagraph (B) and inserting in lieu thereof "individual".

(5) Section 202(f)(4) of such Act is amended—

(A) by striking out "remarries" and inserting in lieu thereof "marries";

(B) by inserting "or a surviving divorced husband," after "age 60,"; and

(C) by inserting "or surviving divorced husband's" after "widower's".

(6) Section 202(e)(3)(A) of such Act is amended by striking out "(f)" and inserting in lieu thereof "(c), (f),".

(7) Section 202(g)(3)(A) of such Act is amended by inserting "(c)," before "(f),".

(8) Section 202(h)(4)(A) of such Act is amended by inserting "(c)," before "(e),".

(c)(1) Section 216(d) of such Act is amended by redesignating paragraph (4) as paragraph (6), and by inserting after paragraph (3) the following new paragraphs:

"(4) The term 'divorced husband' means a man divorced from an individual, but only if he had been married to such individual for a period of 10 years immediately before the date the divorce became effective.

"(5) The term 'surviving divorced husband' means a man divorced from an individual who has died, but only if he had been married to the individual for a period of 10 years immediately before the divorce became effective.".

(2) The heading of section 216(d) of such Act is amended to read as follows:

"Divorced Spouses; Divorce".

(d)(1) Section 205(b) of such Act is amended by inserting "divorced husband," after "husband,", and by inserting "surviving divorced husband," after "widower,".

(2) Section 205(c)(1)(C) of such Act is amended by inserting "surviving divorced husband," after "wife,".

### REMARRIAGE OF SURVIVING SPOUSE BEFORE AGE 60

SEC. 202. Section 202(f)(1)(A) of the Social Security Act is amended by striking out "has not remarried" and inserting in lieu thereof "is not married".

### ILLEGITIMATE CHILDREN

SEC. 203. (a) Section 216(h)(3) of the Social Security Act is amended by inserting "mother or" before "father" wherever it appears.

(b) Section 216(h)(3)(A)(ii) of such Act is amended by striking out all that follows "time" and inserting in lieu thereof "such applicant's application for benefits was filed;".

(c) Section 216(h)(3)(B)(ii) of such Act is amended by striking out "such period of disability began" and inserting in lieu thereof "such applicant's application for benefits was filed".

(d) Section 216(h)(3) of such Act is further amended—

(1) by striking out "his" wherever it appears and inserting in lieu thereof "his or her"; and

(2) by striking out "he" in subparagraph (B) and inserting in lieu thereof "he or she".

### TRANSITIONAL INSURED STATUS

SEC. 204. (a) Section 227(a) of the Social Security Act is amended—

(1) by striking out "wife" wherever it appears and inserting in lieu thereof "spouse";

(2) by striking out "wife's" wherever it appears and inserting in lieu thereof "spouse's";

(3) by striking out "she" wherever it appears and inserting in lieu thereof "he or she";

(4) by striking out "his" and inserting in lieu thereof "the"; and

(5) by inserting "or section 202(c)" after "section 202(b)" wherever it appears.

(b) Section 227(b) and section 227(c) of such Act are amended—

(1) by striking out "widow" wherever it appears and inserting in lieu thereof "surviving spouse";

(2) by striking out "widow's" wherever it appears and inserting in lieu thereof "surviving spouse's";

(3) by striking out "her" wherever it appears and inserting in lieu thereof "the"; and

(4) by inserting "or section 202(f)" after "section 202(e)" wherever it appears.

(c) Section 216 of such Act is amended by inserting before subsection (b) the following new subsection:

"Spouse; Surviving Spouse

"(a)(1) The term 'spouse' means a wife as defined in subsection (b) or a husband as defined in subsection (f).

"(2) The term 'surviving spouse' means a widow as defined in subsection (c) or a widower as defined in subsection (g).".

### EQUALIZATION OF BENEFITS UNDER SECTION 228

SEC. 205. (a) Section 228(b)(2) of the Social Security Act is amended—

(1) by striking out "the husband's benefit" and inserting in lieu thereof "each of their benefits";

(2) by striking out "$64.40" and inserting in lieu thereof "$48.30"; and

(3) by striking out all that follows "section 215(i)" the first time it appears and inserting in lieu thereof a period.

(b) Section 228(c)(3) of such Act is amended to read as follows:

"(3) In the case of a husband or wife, both of whom are entitled to benefits under this section for any month, the benefit amount of each, after any reduction under paragraph (1), shall be further reduced (but not below zero) by the excess (if any) of (A) the total amount of any periodic benefits under governmental pension systems for which the other is eligible for such month, over (B) the larger of $48.30 or the amount most recently established in lieu thereof under section 215(i).".

(c) Section 228 of such Act is further amended—

(1) by striking out "he" wherever it appears in subsection (a) and inserting in lieu thereof "he or she";

(2) by striking out "$32.20" in subsection (c)(2) and inserting in lieu thereof "$48.30"; and

(3) by striking out "his" in subsection (c)(4)(C) and inserting in lieu thereof "his or her".

(d) The Secretary shall increase the amounts specified in section 228 of the Social Security Act, as amended by this section, to take into account any general benefit increases (as referred to in section 215(i)(3) of such Act), and any increases under section 215(i) of such Act, which have occurred after June 1974.

### FATHER'S INSURANCE BENEFITS

SEC. 206. (a) Section 202(g) of the Social Security Act is amended—

(1) by striking out "widow" wherever it appears and inserting in lieu thereof "surviving spouse";

(2) by striking out "widow's" wherever it appears and inserting in lieu thereof "surviving spouse's";

(3) by striking out "wife's insurance benefits" in paragraph (1)(D) and inserting in lieu thereof "a spouse's insurance benefit";

(4) by striking out "her" wherever it appears and inserting in lieu thereof "his or her";

(5) by striking out "she" wherever it appears and inserting in lieu thereof "he or she";

(6) by striking out "mother" wherever it appears and inserting in lieu thereof "parent";

(7) by inserting "or father's" after "mother's" wherever it appears;

(8) by striking out "after August 1950"; and

(9) in paragraph (3)(A) (as amended by section 201(b)(7) of this Act)—

(A) by inserting "this subsection or" before "subsection (a)"; and

(B) by striking out "(c)," and inserting in lieu thereof "(b), (c), (e),".

(b) The heading of section 202(g) of such Act is amended by inserting "and Father's" after "Mother's".

(c) Section 216(d) of such Act (as amended by section 201(c)(1) of this Act) is further amended by redesignating paragraph (6) as paragraph (8) and by inserting after paragraph (5) the following new paragraphs:

"(6) The term 'surviving divorced father' means a man divorced from an individual who has died, but only if (A) he is the father of her son or daughter, (B) he legally adopted her son or daughter while he was married to her and while such son or daughter was under the age of 18, (C) she legally adopted his son or daughter while he was married to her and while such son or daughter was under the age of 18, or (D) he was married to her at the time both of them legally adopted a child under the age of 18.

"(7) The term 'surviving divorced parent' means a surviving divorced mother as defined in paragraph (3) of this subsection or a surviving divorced father as defined in paragraph (6).".

(d) Section 202(c)(1) of such Act (as amended by section 201(a) of this Act) is further amended by inserting "(subject to subsection (s))" before "be entitled to" in the matter following subparagraph (D) and preceding subparagraph (E).

(e) Section 202(c)(1)(B) of such Act is amended by inserting after "62" the following: "or (in the case of a husband) has in his care (individually or jointly with such individual) at the time of filing such application a child entitled to child's insurance benefits on the basis of the wages and self-employment income of such individual".

(f) Section 202(c)(1) of such Act (as amended by section 201(a) of this Act and the preceding provisions of this section) is further amended by redesignating the new subparagraphs (I) and (J) as subparagraphs (J) and (K), respectively, and by inserting after subparagraph (H) the following new subparagraph:

"(I) in the case of a husband who has not attained age 62, no child of such individual is entitled to a child's insurance benefit,".

(g) Section 202(f)(1)(C) of such Act is amended by inserting "(i)" after "(C)", by inserting "or" after "223,", and by adding at the end thereof the following new clause:

"(ii) was entitled, on the basis of such wages and self-employment income, to father's insurance benefits for the month preceding the month in which he attained age 65, and".

(h) Section 202(f)(6) of such Act is amended by striking out "or" at the end of subparagraph (A), by redesignating subparagraph (B) as subparagraph (C), and by inserting immediately after subparagraph (A) the following new subparagraph:

"(B) the last month for which he was entitled to father's insurance benefits on the basis of the wages and self-employment income of such individual, or".

(i) Section 203(f)(1)(F) of such Act is amended by striking out "section 202(b) (but only by reason of having a child in her care within the meaning of paragraph (1)(B) of that subsection)" and inserting in lieu thereof "section 202(b) or (c) (but only by reason of having a child in his or her care within the meaning of paragraph (1)(B) of subsection (b) or (c), as may be applicable)".

### EFFECT OF MARRIAGE ON CHILDHOOD DISABILITY BENEFICIARY

SEC. 207. (a) Section 202(d)(5) of the Social Security Act (as amended by section 201(a)(8) of this Act) is further amended—

(1) by striking out "a male individual" in the matter following subparagraph (B) and inserting in lieu thereof "an individual";

(2) by striking out "he" each place it appears and inserting in lieu thereof "such individual"; and

(3) by striking out "his" and inserting in lieu thereof "such individual's".

(b) The amendments made by subsection (a) shall apply with respect to benefits under title II of the Social Security Act for months after the month in which this Act is enacted, but only in cases in which the "last month" referred to in section 202(d)(5) of such Act is a month after the month in which this Act is enacted.

EFFECT OF MARRIAGE ON OTHER BENEFITS OF DEPENDENTS OR SURVIVORS

SEC. 208. (a) Section 202(c)(4) of the Social Security Act (as added by section 201(a)(4) of this Act) is amended by inserting before the period at the end thereof the following: "; except that, in the case of such a marriage to an individual entitled to benefits under subsection (d), the preceding provisions of this paragraph shall not apply with respect to benefits for months after the last month for which such individual is entitled to such benefits under subsection (d) unless she ceases to be so entitled by reason of her death".

(b) Section 202(f)(4) of such Act is amended by inserting before the period at the end thereof the following: "; except that, in the case of such a marriage to an individual entitled to benefits under subsection (d), the preceding provisions of this paragraph shall not apply with respect to benefits for months after the last month for which such individual is entitled to such benefits under subsection (d) unless she ceases to be so entitled by reason of her death".

(c) Section 202(h)(4) of such Act is amended—

(1) by striking out "a male individual" in the matter following clause (B) and inserting in lieu thereof "an individual"; and

(2) by striking out "he" and "his" and inserting in lieu thereof "such individual" and "such individual's", respectively.

(d) The amendments made by this section shall apply with respect to benefits under title II of the Social Security Act for months after the month in which this Act is enacted, but only in cases in which the "last month" referred to in section 202(c)(4), 202(f)(4), 202(g)(3), or 202(h)(4) of such Act is a month after the month in which this Act is enacted.

### TREATMENT OF SELF-EMPLOYMENT INCOME IN COMMUNITY PROPERTY STATES

SEC. 209. (a) Section 211(a)(5)(A) of the Social Security Act and section 1402(a)(5)(A) of the Internal Revenue Code of 1954 are each amended by striking out "husband unless the wife exercises substantially all of the management and control of such trade or business, in which case all of such gross income and deductions shall be treated as the gross income and deductions of the wife" and inserting in lieu thereof "spouse who is carrying on the trade or business without regard to whether such income is community income".

(b) The amendments made by subsection (a) shall apply with respect to taxable years that include the month of October 1980 or any subsequent month.

### CREDIT FOR CERTAIN MILITARY SERVICE

SEC. 210. Section 217(f) of the Social Security Act is amended—

(1) by striking out "widow" each place it appears and inserting in lieu thereof "surviving spouse"; and

(2) by striking out "his" and "her" wherever they appear (except in clause (A) of paragraph (1)) and inserting in lieu thereof in each instance "his or her".

### CONFORMING AMENDMENTS

SEC. 211. (a) Section 202(b)(3)(A) of the Social Security Act (as amended by section 201(a)(6) of this Act) and section 202(e)(3)(A) of such Act (as amended by section 201(b)(6) of this Act) are each further amended by inserting "(g)," after "(f),".

(b) Section 202(q)(3) of such Act is amended by inserting "or surviving divorced husband" after "widower" in subparagraphs (E), (F), and (G).

(c) Section 202(q)(5) of such Act is amended—

(1) by inserting "or husband's" after "wife's" wherever it appears;

(2) by striking out "her" in subparagraph (A)(i) and inserting in lieu thereof "him or her";

(3) by striking out "her" the second place it appears in subparagraph (A)(ii) and inserting in lieu thereof "the";

(4) by striking out "she" wherever it appears and inserting in lieu thereof "he or she";

(5) by striking out "her" wherever it appears (except where paragraphs (2) and (3) of this subsection apply) and inserting in lieu thereof "his or her";

(6) by striking out "the woman" in subparagraph (B)(ii) and "a woman" in subparagraph (C) and inserting in lieu thereof "the individual" and "an individual", respectively; and

(7) in subparagraph (D)—

(A) by inserting "or widower's" after "widow's";

(B) by striking out "husband" wherever it appears and inserting in lieu thereof "spouse";;

(C) by striking out "husband's" wherever it appears and inserting in lieu thereof "spouse's"; and

(D) by inserting "or father's" after "mother's".

(d)(1) Section 202(q)(6)(A)(i) of such Act is amended by striking out "or husband's" in subdivision (I), and by inserting "or husband's" after "wife's" in subdivision (II).

(2) Section 202(q)(7) of such Act is amended—

(A) in subparagraph (B), by inserting "or husband's" after "wife's", by striking out "she" and inserting in lieu thereof "such individual", and by inserting "his or" before "her", and

(B) in subparagraph (D), by inserting "or widower's" after "widow's".

(e)(1) Section 202(s)(1) of such Act is amended by inserting "(c)(1)," after "(b)(1),".

(2) Section 202(s)(2) of such Act is amended by inserting "(c)(4)," after "(b)(3),".

(3) Section 202(s)(3) of such Act is amended by inserting "(c)(4)," after "(b)(3),", and by inserting "(f)(4)," after "(e)(3),".

(f) The third sentence of section 203(b) of such Act is amended by inserting "or father's" after "mother's".

(g) Section 203(c) of such Act is amended to read as follows:

### "Deductions on Account of Noncovered Work Outside the United States or Failure to Have Child in Care

"(c) Deductions, in such amounts and at such time or times as the Secretary shall determine, shall be made from any payment or payments under this title to which an individual is entitled, until the total of such deductions equals such individual's benefits or benefit under section 202 for any month—

"(1) in which such individual is under the age of seventy and for more than forty-five hours of which such individual engaged in noncovered remunerative activity outside the United States;

"(2) in which such individual, if a wife or husband under age sixty-five entitled to a wife's or husband's insurance benefit, did not have in his or her care (individually or jointly with his or her spouse) a child of such spouse entitled to a child's insurance benefit and such wife's or husband's insurance benefit for such month was not reduced under the provisions of section 202(q);

"(3) in which such individual, if a widow or widower entitled to a mother's or father's insurance benefit, did not have in his or her care a child of his or her deceased spouse entitled to a child's insurance benefit; or

"(4) in which such an individual, if a surviving divorced mother or father entitled to a mother's or father's insurance benefit, did not have in his or her care a child of his or her deceased former spouse who (A) is his or her son, daughter, or legally adopted child and (B) is entitled to a child's insurance benefit on the basis of the wages and self-employment income of such deceased former spouse.

For purposes of paragraphs (2), (3), and (4) of this subsection, a child shall not be considered to be entitled to a child's insurance benefit for any month in which paragraph (1) of section 202(s) applies or an event specified in section 222(b) occurs with respect to such child. Subject to paragraph (3) of such section 202(s), no deduction shall be made under this subsection from any child's insurance benefit for the month in which the child entitled to such benefit attained the age of eighteen or any subsequent month; nor shall any deduction be made under this subsection from any widow's insurance benefit for any month in which the widow or surviving divorced wife is entitled and has not attained age 65 (but only if she became so entitled prior to attaining age 60), or from any widower's insurance benefit for any month in which the widower or surviving divorced husband is entitled and has not attained age 65 (but only if he became so entitled prior to attaining age 60).".

(h) Section 203(d) of such Act is amended by inserting "divorced husband," after "husband," in paragraph (1), and by inserting "or father's" after "mother's" each place it appears in paragraph (2).

(i)(1) Section 205(b) of such Act (as amended by section 201(d)(1) of this Act) is further amended by inserting "surviving divorced father," after "surviving divorced mother,".

(2) Section 205(c)(1)(C) of such Act (as amended by section 201(d)(2) of this Act) is further amended by inserting "surviving divorced father," after "surviving divorced mother,".

(j) Section 216(f)(3)(A) of such Act is amended by inserting "(c)," before "(f)",

(k) Section 216(g)(6)(A) of such Act is amended by inserting "(c)," before "(f)".

(l) Section 222(b)(1) of such Act is amended by striking out "or surviving divorced wife" and inserting in lieu thereof ", surviving divorced wife, or surviving divorced husband".

(m) Section 222(b)(2) of such Act is amended by inserting "or father's" after "mother's" wherever it appears.

(n) Section 222(b)(3) of such Act is amended by inserting "divorced husband," after "husband,".

(o) Section 223(d)(2) of such Act is amended by striking out "or widower" in subparagraphs (A) and (B) and inserting in lieu thereof "widower, or surviving divorced husband".

(p) Section 225(a) of such Act is amended by inserting "or surviving divorced husband" after "widower".

(q)(1) Section 226(e)(3) of such Act is amended to read as follows:

"(3) For purposes of determining entitlement to hospital insurance benefits under subsection (b), any disabled widow aged 50 or older who is entitled to mother's insurance benefits (and who would have been entitled to widow's insurance benefits by reason of disability if she had filed for such widow's benefits), and any disabled widower aged 50 or older who is entitled to father's insurance benefits (and who would have been entitled to widower's insurance benefits by reason of disability if he had filed for such widower's benefits), shall, upon application for such hospital insurance benefits be deemed to have filed for such widow's or widower's insurance benefits.".

(2) For purposes of determining entitlement to hospital insurance benefits under section 226(e)(3) of such Act, as amended by paragraph (1), an individual becoming entitled to such hospital insurance benefits as a result of the amendment made by such paragraph shall, upon furnishing proof of his or her disability within twelve months after the month in which this Act is enacted, under such procedures as the Secretary of Health and Human Services may prescribe, be deemed to have been entitled to the widow's or widower's benefits re-

ferred to in such section 226(e)(3), as so amended, as of the time such individual would have been entitled to such widow's or widower's benefits if he or she had filed a timely application therefor.

### EFFECTIVE DATE OF TITLE II

SEC. 212. (a) Except as otherwise specifically provided in this title, the amendments made by this title apply only with respect to monthly benefits payable under title II of the Social Security Act for months after the month in which this Act is enacted.

(b) Nothing in any amendment made by this title shall be construed as affecting the validity of any benefit which was paid, prior to the effective date of such amendment, as a result of a judicial determination.

## TITLE III—COVERAGE

### COVERAGE OF EMPLOYEES OF FOREIGN AFFILIATES OF AMERICAN EMPLOYERS

SEC. 301. (a)(1) Section 210(a) of the Social Security Act is amended by striking out "of a domestic corporation (as determined in accordance with section 7701 of the Internal Revenue Code of 1954)" in the matter preceding paragraph (1) and inserting in lieu thereof "of an American employer (as defined in subsection (e))".

(2)(A) Section 3121(l) of the Internal Revenue Code of 1954 is amended—

(i) in the heading, by striking out "DOMESTIC CORPORATIONS" and inserting in lieu thereof "AMERICAN EMPLOYERS";

(ii) in paragraph (1)—

(I) in the matter preceding subparagraph (A)—

(a) by striking out "any domestic corporation" and inserting in lieu thereof "any American employer (as defined in subsection (h))",

(b) by striking out "such corporation" and inserting in lieu thereof "such employer", and

(c) by striking out "such domestic corporation" and inserting in lieu thereof "such American employer", and

(II) in subparagraphs (A) and (B), by striking out "the domestic corporation" wherever it appears and inserting in lieu thereof "the American employer";

(iii) in paragraph (3)—

(I) by striking out "A DOMESTIC CORPORATION" in the heading and inserting in lieu thereof "AMERICAN EMPLOYER", and

(II) by striking out "the domestic corporation" wherever it appears and inserting in lieu thereof "the American employer";

(iv) in the last sentence of paragraph (4) and in the matter in paragraph (8) preceding subparagraph (A), by striking out "a domestic corporation" and inserting in lieu thereof "an American employer";

(v) in paragraphs (4), (5), and (8), by striking out "domestic corporation" wherever it appears (except where clause (iv) of this subparagraph applies) and inserting in lieu thereof "American employer";

(vi) in paragraph (9)—

(I) by striking out "DOMESTIC CORPORATION" in the heading and inserting in lieu thereof "AMERICAN EMPLOYER", and

(II) by striking out "Each domestic corporation" and inserting in lieu thereof "Each American employer"; and

(vii) in paragraph (10), by striking out "on domestic corporations" and inserting in lieu thereof "on American employers".

(B) Section 6413(c)(2)(C) of such Code is amended by striking out "domestic corporation" and inserting in lieu thereof "American employer".

(C) Section 1402(b) of such Code is amended by striking out "domestic corporations" and inserting in lieu thereof "American employers".

(D) Section 406 of such Code is amended—

(i) in the heading of subsection (a), by striking out "DOMESTIC CORPORATION" and inserting in lieu thereof "AMERICAN EMPLOYER",

(ii) in subsection (a), by striking out "a domestic corporation" and inserting in lieu thereof "an American employer (as defined in section 3121(h))";

(iii) in the remaining subsections, by striking out "a domestic corporation" wherever it appears and inserting in lieu thereof "an American employer";

(iv) by striking out "such domestic corporation" and "the domestic corporation" wherever they appear and inserting in lieu thereof "such American employer" and "the American employer", respectively;

(v) in subsection (c)(3), by striking out "another corporation" and inserting in lieu thereof "another trade or business"; and

(vi) in subsection (d)—

(I) in the matter preceding paragraph (1), by striking out "another corporation" and inserting in lieu thereof "a corporation", and

(II) in paragraph (1), by striking out "any other corporation" and inserting in lieu thereof "any other trade or business".

(b)(1) Section 210(a) of the Social Security Act (as amended by subsection (a)(1) of this section) is further amended by striking out "subsidiary" wherever it appears in the matter preceding paragraph (1) and inserting in lieu thereof "affiliate".

(2)(A) Section 3121(l)(8) of the Internal Revenue Code of 1954 is amended—

(i) in the heading, by striking out "SUBSIDIARY" and inserting in lieu thereof "AFFILIATE";

(ii) in the matter preceding subparagraph (A), by striking out "subsidiary" and inserting in lieu thereof "affiliate";

(iii) in subparagraph (A), by striking out "corporation not less than 20 percent of the voting stock" and inserting in lieu thereof "trade or business not less than 10 percent"; and

(iv) by amending subparagraph (B) to read as follows:

"(B) a foreign trade or business that is owned by or related to a foreign trade or business described in subparagraph (A), if the percentage of that ownership or relationship, when multiplied by actual ownership percentage determined under that subparagraph, is not less than 10 percent.".

(B)(i) Section 3121(l) of such Code (other than paragraph (8)) is amended—

(I) by striking out "SUBSIDIARIES" in the heading and inserting in lieu thereof "AFFILIATES";

(II) by striking out "SUBSIDIARIES" in the heading of paragraph (1) and inserting in lieu thereof "AFFILIATES"; and

(III) by striking out "subsidiary" and "subsidiaries" wherever they appear and inserting in lieu thereof "affiliate" and "affiliates", respectively.

(ii) Section 3121(l) of such Code is further amended by striking out "foreign corporation" wherever it appears in paragraph (3) and inserting in lieu thereof "foreign trade or business", and by striking out "foreign corporations" in paragraph (9) and inserting in lieu thereof "foreign trades or businesses".

(C) Sections 6413(c)(2) and 6413(c)(2)(C) of such Code are each amended by striking out "FOREIGN CORPORATIONS" in the heading and inserting in lieu thereof "FOREIGN TRADES OR BUSINESSES".

(D) Section 1402(b) of such Code is amended by striking out "subsidiaries" and inserting in lieu thereof "affiliates".

(E)(i) Section 406 of such Code is amended—

(I) by striking out "**SUBSIDIARIES**" in the heading and inserting in lieu thereof "**AFFILIATES**", and

(II) by striking out "foreign subsidiaries" and "foreign subsidiary" wherever they appear and inserting in lieu thereof "foreign affiliates" and "foreign affiliate", respectively.

(ii) The table of sections for subpart A of part I of subchapter D of chapter 1 of such Code is amended by striking out "subsidiaries" in the item relating to section 406 and inserting in lieu thereof "affiliates".

(c) The amendments made by subsections (a) and (b) shall be effective on the date of the enactment of this Act.

### EXTENSION OF COVERAGE BY INTERNATIONAL SOCIAL SECURITY AGREEMENT

SEC. 302. (a)(1) Section 210(a) of the Social Security Act is amended, in the matter preceding paragraph (1)—

(A) by striking out "either" before "(A)", and

(B) by inserting before "; except" the following: ", or (C) if it is service, regardless of where or by whom performed, which is designated as employment or recognized as equivalent to employment under an agreement entered into under section 233".

(2) Section 3121(b) of the Internal Revenue Code of 1954 is amended, in the matter preceding paragraph (1)—

(A) by striking out "either" before "(A)", and

(B) by inserting before "; except" the following: ", or (C) if it is service, regardless of where or by whom performed, which is designated as employment or recognized as equivalent to employment under an agreement entered into under section 233 of the Social Security Act".

(b)(1) Section 211(b) of the Social Security Act is amended by inserting after "non-resident alien individual" the following: ", except as provided by an agreement under section 233".

(2) The first sentence of section 1402(b) of the Internal Revenue Code of 1954 is amended by inserting after "non-resident alien individual" the following: ", except as provided by an agreement under section 233 of the Social Security Act".

(c) The amendments made by this section shall be effective for taxable years beginning on or after the date of the enactment of this Act.

## FOREIGN EARNED INCOME EXCLUSION FROM NET SELF-EMPLOYMENT INCOME

SEC. 303. (a) Section 211(a)(10) of the Social Security Act is amended to read as follows:

"(10) In the case of an individual described in section 911(d)(1)(B) of the Internal Revenue Code of

1954, the exclusion from gross income provided by section 911(a)(1) of such Code shall not apply; and".

(b) The amendment made by subsection (a) shall apply with respect to taxable years beginning after December 31, 1981.

### SOCIAL SECURITY TAX TREATMENT OF CASH OR DEFERRED COMPENSATION ARRANGEMENTS

SEC. 304. (a)(1) Section 209(e)(1) of the Social Security Act is amended by inserting "a payment to a trust which is part of a qualified cash or deferred arrangement (as defined in section 401(k)(2) of the Internal Revenue Code of 1954) or is" after "unless such payment is".

(2) Section 3121(a)(5)(A) of the Internal Revenue Code of 1954 is amended by inserting "a payment to a trust which is part of a qualified cash or deferred arrangement (as defined in section 401(k)(2)) or is" after "unless such payment is".

(b) Section 402(a)(8) of the Internal Revenue Code of 1954 is amended by inserting "(other than section 3121(a)(5)(A))" after "For purposes of this title".

(c) The amendments made by this section shall apply with respect to payments and contributions made in calendar years beginning more than six months after the date of the enactment of this Act.

## TREATMENT OF PAY AFTER AGE 62 AS WAGES

SEC. 305. (a) Section 209 of the Social Security Act is amended by striking out subsection (i).

(b) Section 3121(a) of the Internal Revenue Code of 1954 is amended by striking out paragraph (9).

(c) The amendments made by this section shall apply with respect to calendar years beginning more than six months after the date of the enactment of this Act.

## PAYMENTS UNDER SIMPLIFIED EMPLOYEE PENSION PLANS EXCLUDED FROM WAGES FOR PURPOSES OF BENEFIT COMPUTATION

SEC. 306. (a) Section 209(e) of the Social Security Act is amended by striking out "1954;" and inserting in lieu thereof the following: "1954, or (5) under a simplified employee pension if, at the time of the payment, it is reasonable to believe that the employee will be entitled to a deduction under section 219 of the Internal Revenue Code of 1954 for such payment;".

(b) The amendment made by subsection (a) shall apply with respect to payments made after the date of the enactment of this Act.

## EFFECT OF CHANGES IN NAMES OF STATE AND LOCAL EMPLOYEE GROUPS IN UTAH

SEC. 307. (a) Section 218(o) of the Social Security Act is amended by adding at the end thereof the following new sentence: "Coverage provided for in this subsection shall not be affected by a subsequent change in the name of a group.".

(b) The amendment made by subsection (a) shall apply with respect to name changes made before, on, or after the date of the enactment of this section.

# TITLE IV—MISCELLANEOUS AND TECHNICAL AMENDMENTS

## TECHNICAL AND CONFORMING AMENDMENTS TO MAXIMUM FAMILY BENEFIT PROVISIONS

SEC. 401. (a)(1) Section 203(a)(3)(A) of the Social Security Act is amended by striking out clause (ii) and inserting in lieu thereof the following:

"(ii) an amount (I) initially equal to the product of 1.75 and the primary insurance amount that would be computed under section 215(a)(1), for January of the year determined for purposes of this clause under the following two sentences, with respect to average indexed monthly earnings equal to one-twelfth of the contribution and benefit base determined for that year under section 230, and (II) thereafter increased in accordance with the provisions of section 215(i)(2)(A)(ii).

The year established for purposes of clause (ii) shall be 1983 or, if it occurs later with respect to any individual, the year in which occurred the month that the application of the reduction provisions contained in this subparagraph began with respect to benefits payable on the basis of the wages and self-employment income of the insured individual. If for any month subsequent to the first month for which clause (ii) applies (with respect to benefits payable on the basis of the wages and self-employment income of the insured individual) the reduction under this subparagraph ceases to apply, then the year determined under the preceding sentence shall be redetermined (for purposes of any subsequent application of this subparagraph with respect to benefits payable on the basis of such wages and self-employment income) as though this subparagraph had not been previously applicable.".

(2) Section 203(a)(7) of such Act is amended by striking out everything that follows "shall be reduced to an amount equal to" and inserting in lieu thereof "the amount determined in accordance with the provisions of paragraph (3)(A)(ii) of this subsection, except that for this purpose the references to subparagraph (A) in the last two sentences of paragraph (3)(A) shall be deemed to be references to paragraph (7).".

(b) Clause (A) in the last sentence of section 203(b) of such Act is amended by striking out "penultimate sentence" and inserting in lieu thereof "first sentence of paragraph (4)".

(c) The amendments made by subsection (a) shall be effective with respect to payments made for months after December 1983.

### APPLICATION OF SOCIAL SECURITY PROGRAM TO NORTHERN MARIANA ISLANDS

SEC. 402. Subsection (b) of section 606 of the Covenant to Establish a Commonwealth of the Northern Mariana Islands in Political Union With the United States of America, approved by Public Law 94-241, is amended by striking out "upon termination of the Trusteeship Agreement or" and inserting in lieu thereof "on January 1 of the first calendar year following the termination of the Trusteeship Agreement or upon".

### SIMPLIFICATION OF TRUST FUND REIMBURSEMENT COMPUTATION WITH RESPECT TO BENEFITS ATTRIBUTABLE TO NONCONTRIBUTORY WAGE CREDITS FOR MILITARY SERVICE

SEC. 403. (a) The first sentence of section 217(g)(1) of the Social Security Act is amended by inserting before the period at the end thereof the following: "; except that with respect to benefits paid during any fiscal year beginning after September 30, 1976, the Secretary shall exclude amounts attributable to benefits paid during the fiscal year to an individual on account of this section if benefits were also paid to the individual during the fiscal year on account of section 229".

(b) Section 229(b) of such Act is amended—

(1) in clause (1), by inserting after the second comma the following: "or from subsection (a) and section 217 except insofar as those costs are included in the Secretary's determination under section 217(g)(1),"; and

(2) by striking out the last sentence.

### REDUCTION FROM 72 TO 70 OF AGE BEYOND WHICH NO DELAYED RETIREMENT CREDITS CAN BE EARNED

SEC. 404. (a) Section 202(w) of the Social Security Act is amended—

(1) in paragraph (2)(A), by striking out "age 72" and inserting in lieu thereof "age 70"; and

(2) in paragraph [illegible] striking out "age 72 after 1972" and inserting in [illegible]reof "age 70".

(b) The amendments [illegible]bsection (a) shall apply with respect to individuals [illegible] age 70 after December 1982. For individuals who attain age 70 before January 1983, section 202(w) as in effect immediately before the enactment of the amendments made by this section shall apply, except that no increment months as determined under such section attributable to months after December 1982 shall accrue.

### RELAXATION OF INSURED STATUS REQUIREMENTS FOR CERTAIN WORKERS PREVIOUSLY ENTITLED TO A PERIOD OF DISABILITY

SEC. 405. (a) Section 216(i)(3)(B) of the Social Security Act is amended—

(1) by striking out the semicolon at the end of clause (ii) and inserting in lieu thereof ", or"; and

(2) by inserting after clause (ii) the following new clause:

"(iii) in the case of an individual (not otherwise insured under clause (i)) who, by reason of clause (ii), had a prior period of disability that began during a period before the quarter in which he or she attained age 31, not less than one-half of the quarters beginning after such individual attained age 21 and ending with such quarter are quarters of coverage;".

(b) Section 223(c)(1)(B) of such Act is amended—

(1) by striking out the semicolon at the end of clause (ii) and inserting in lieu thereof ", or"; and

(2) by inserting after clause (ii) the following new clause:

"(iii) in the case of an individual (not otherwise insured under clause (i)) who, by reason of section 216(i)(3)(B)(ii), had a prior period of disability that began during a period before the quarter in which he or she attained age 31, not less than one-half of the quarters beginning after such individual attained age 21 and ending with such quarter are quarters of coverage;".

(c) The amendments made by this section shall be effective with respect to applications for disability insurance benefits under section 223 of the Social Security Act, and for disability determinations under section 216(i) of such Act, filed after the date of the enactment of this Act, except that no monthly benefits under title II of the Social Security Act shall be payable or increased by reason of the amendments made by this section for months before the month following the month of enactment of this Act.

### PROTECTION OF BENEFITS OF ILLEGITIMATE CHILDREN OF DISABLED BENEFICIARIES

SEC. 406. (a) The last sentence of section 216(h)(3) of the Social Security Act is amended by striking out "subparagraph (A)(i)" and inserting in lieu thereof "subparagraphs (A)(i) and (B)(i)".

(b) The amendment made by subsection (a) shall be effective on the date of the enactment of this Act.

### CONTINUATION OF BENEFITS OF DISABLED WIDOW OR WIDOWER WHO MARRIES A RETIRED OR DISABLED WORKER

SEC. 407. (a) Section 202(e)(3) of the Social Security Act (as amended by sections 201(b)(6) and 211(a) of this Act) is further amended—

(1) in subparagraph (A), by inserting "(a)," after "subsection", and by striking out "or" the second place it appears;

(2) by adding "or" after the comma at the end of subparagraph (B); and

(3) by inserting immediately after subparagraph (B) the following new subparagraph:

"(C) an individual entitled to benefits under section 223(a),".

(b) Section 202(f)(4) of such Act (as amended by sections 201(b)(5) and 208(b) of this Act) is further amended—

(1) in subparagraph (A), by inserting "(a)," after "subsection", and by striking out "or" the second place it appears;

(2) in subparagraph (B) by adding "or" after the comma at the end of subparagraph (B); and

(3) by inserting immediately after subparagraph (B) the following new subparagraph:

"(C) an individual entitled to benefits under section 223(a),".

(c) The amendments made by this section shall apply with respect to benefits payable for months beginning after the date of the enactment of this Act.

### ONE-MONTH RETROACTIVITY OF WIDOW'S AND WIDOWER'S INSURANCE BENEFITS

SEC. 408. (a) Section 202(j)(4)(B) of the Social Security Act is amended—

(1) by redesignating clauses (iii) and (iv) as clauses (iv) and (v), respectively; and

(2) by adding after clause (ii) the following new clause:

"(iii) Subparagraph (A) does not apply to a benefit under subsection (e) or (f) for the month immediately preceding the month of application, if the insured individual died in that preceding month.".

(b) The amendments made by subsection (a) shall apply with respect to survivors whose applications for monthly benefits are filed after the second month following the month in which this Act is enacted.

### NON-ASSIGNABILITY OF BENEFITS

SEC. 409. (a) Section 207 of the Social Security Act is amended—

(1) by inserting "(a)" before "The right"; and

(2) by adding at the end thereof the following new subsection:

"(b) No other provision of law, enacted before, on, or after the date of the enactment of this section, may be construed to limit, supersede, or otherwise modify the provisions of this section except to the extent that it does so by express reference to this section.".

(b) The amendments made by subsection (a) shall apply only with respect to benefits payable or rights existing under title II of the Social Security Act on or after the date of the enactment of this Act.

### REQUIREMENT OF PREVIOUS UNITED STATES RESIDENCY FOR ALIEN DEPENDENTS AND SURVIVORS LIVING OUTSIDE THE UNITED STATES

SEC. 410. (a) Section 202(t) of the Social Security Act is amended—

(1) in the heading, by adding after "United States" the following: "; Residency Requirements for Dependents and Survivors"; and

(2) by adding at the end thereof the following new paragraph:

"(11)(A) Paragraph (2) and subparagraphs (A), (B), (C), and (E) of paragraph (4) shall apply with respect to an individual's monthly benefits under subsection (b), (c), (d), (e), (f), (g), or (h) only if such individual meets the residency requirements of this paragraph with respect to those benefits.

"(B) An individual entitled to benefits under subsection (b), (c), (e), (f), or (g) meets the residency requirements of this paragraph with respect to those benefits only if such individual has resided in the United States, and while so residing bore a spousal relationship to the person on whose wages and self-employment income such entitlement is based, for a total period of not less than 5 years. For purposes of this subparagraph, a period of time for which an individual bears a spousal relationship to another person consists of a period throughout which the individual has been, with respect to such other person, a wife, a husband, a widow, a widower, a divorced wife, a divorced husband, a surviving divorced wife, a surviving divorced husband, a surviving divorced mother, a surviving divorced father, or (as applicable in the course of such period) any two or more of the foregoing.

"(C) An individual entitled to benefits under subsection (d) meets the residency requirements of this paragraph with respect to those benefits only if—

"(i)(I) such individual has resided in the United States (as the child of the person on whose wages and self-employment income such entitlement is based) for a total period of not less than 5 years, or

"(II) the person on whose wages and self-employment income such entitlement is based, and the individual's other parent (within the meaning of subsection (h)(3)), if any, have each resided in the United States for a total period of not less than 5 years (or died while residing in the United States), and

"(ii) in the case of an individual entitled to such benefits as an adopted child, such individual was adopted within the United States by the person on whose wages and self-employment income such entitlement is based, and has lived in the United States with such person and received at least one-half of his or her support from such person for a period (beginning before such individual attained age 18) consisting of—

"(I) the year immediately before the month in which such person became entitled to old-age insurance benefits or disability insurance benefits or died, or

"(II) if such person had a period of disability which continued until he or she became entitled to old-age insurance benefits or disability insurance benefits or died, the year immediately before the month in which such period of disability began.

"(D) An individual entitled to benefits under subsection (h) meets the residency requirements of this paragraph with respect to those benefits only if such individual has resided in the United States, and while so residing was a parent (within the meaning of subsection (h)(3)) of the person on whose wages and self-employment income such entitlement is based, for a total period of not less than 5 years.

"(E) This paragraph shall not apply with respect to any individual who is a citizen or resident of a foreign country with which the United States has an agreement in force concluded pursuant to section 233, except to the extent provided by such agreement.".

(b) Paragraphs (2) and (4) of section 202(t) of such Act are each amended by striking out "Paragraph (1) shall not apply" and inserting in lieu thereof "Subject to paragraph (11), paragraph (1) shall not apply".

(c) The amendments made by this section shall apply with respect to benefits for which applications are filed on or after the first day of the sixth month which begins after the date of the enactment of this Act.

Chairman PICKLE. We will ask the subcommittee to come to order and ask our guests to take a seat.

I wish to make a preliminary statement to the Members and to the guests. Today we are taking testimony on H.R. 7326, the Social Security Miscellaneous Technical Improvements Act of 1982.

The purpose of this hearing is to review a series of amendments to the Social Security Act on which there is widespread consensus. A number of these changes have been around for several years.

The only reason they haven't been enacted is primarily that they are not big enough to move on their own, and they are so small they are forgotten about when work begins on major legislation.

The purpose of this legislation is not to make any dramatic changes in the social security system. It does not address the financing problems of social security.

My current intention on this bill is not to press for its passage during the lame-duck session. Rather, after this hearing, I will seek an agreement that if the subcommittee agrees to a particular provision, it be set aside for the next Congress, and included in the final title of next year's social security legislation. I am mindful of the fact that one Congress cannot bind another to action. However, if we do not take this action, I fear that next year, as has happened in previous years, the pressure of considering more significant legislation will divert our attention from these relatively minor yet necessary and important changes.

Following this proposed course of action, action will allow us to properly consider these changes, and then set them aside as we undertake the task of restoring financial solvency to the social security system in the next Congress.

Our first witness will be the Deputy Commissioner for Programs and Policy of the Social Security Administration, Mr. Paul Simmons. We will ask him to come to the witness table first. Social Security Administration Commissioner, Mr. Jack Svahn, is out of the State, and Mr. Simmons is now presenting testimony in behalf of the SSA. He is a good friend of this committee, has been with us on several occasions, and we will be glad to hear from him.

Do you wish to make any additional comments at this time, Mr. Gradison, before we proceed?

Mr. GRADISON. No, thank you.

Chairman PICKLE. Mr. Simmons, would you proceed?

## STATEMENT OF PAUL SIMMONS, DEPUTY COMMISSIONER FOR PROGRAMS AND POLICY, SOCIAL SECURITY ADMINISTRATION, ACCOMPANIED BY LOUIS D. ENOFF, DEPUTY TO THE DEPUTY COMMISSIONER; MARY ROSS, LEGISLATIVE REFERENCE OFFICER; AND LUCIA SWANSON, DEPUTY CHIEF, COVERAGE BRANCH, OFFICE OF LEGISLATIVE AND REGULATORY POLICY

Mr. SIMMONS. Thank you, Mr. Chairman. I am accompanied today by Louis D. Enoff, who is my Deputy, and Mary Ross, Director of our Legislative Reference Office and, as you know, one of the foremost experts on such things as these proposed amendments.

I am sure that every witness who appears before this committee says he or she is pleased to have an opportunity to comment on this, that, and the other thing. In this case it is a true statement. It is seldom that any social security bill could evoke so little controversy as this one does and could do so much to take care of some small problems in the Social Security Act which have grown up over the years.

While most of the provisions of this bill will not affect great numbers of people or have a major impact on program expenditures, the bill would correct a number of inequities and technical problems and anomalies that are in the act. Taken together, these changes are important to the efficiency of the program as a whole, and would be helpful in simplifying some aspects of the system. I was struck this morning in looking at the compilation of social security laws, there are about 1,850 pages in it and the legislative history of the Social Security Act runs to 45 volumes over the past 46 years.

And I am reminded of a remark that Wilbur Cohen once said to me. He said in the time that he had been involved with social security he had personally met 8,000 people who were the original authors of the act. Sometimes when you look at the size of the act, the legislative history, you can believe there are 8,000.

The bill is divided into four titles, which I will discuss in turn. I will not hit every single facet of the bill but hit on some of the most complex features of the bill to help people understand how it would work.

The first title, relating to cash management, section 101, would provide that the trust funds of the social security system be credited with an amount equal to the social security checks which have remained unnegotiated for a year. They represent payments from the social security trust funds. When these checks are not cashed by recipients, the unnegotiated amounts outstanding remain in the general fund of the Treasury under current law, and I understand that practice goes way back. We estimate that unnegotiated social security checks cumulatively total something on the order of $325 million, and that unnegotiated checks will cost the trust funds about $30 million per year in the future.

We understand the National Commission on Social Security Reform is addressing this issue, and we will, of course, wish to consider any recommendations they may make.

We also will, of course, defer to Treasury on their idea of the most effective cash management practices to handle the uncashed check problem.

With respect to section 102, we welcome the opportunity for a study by HHS and Treasury of options for adjusting the float allowance between the time social security checks are issued and the time the trust funds are drawn down to cover Treasury payment of the checks. We share the concern of the HHS Inspector General that current float procedures do not reflect the actual banking practices of social security beneficiaries.

While we are eager to explore modifications of the float period allowed by Treasury in order to enhance the interest earnings of the trust funds, we defer to the Treasury whose Secretary is managing trustee of the trust funds, on this issue.

Section 103 of the bill would require that special obligations issued exclusively to the social security trust funds have short-term interest rates—and maturity dates—when such rates are more favorable than long-term rates, as has been the case over much of the last few years.

Under present law, the rate of interest earned by special issues of the trust funds is equal to the average market yield on all marketable interest-bearing obligations of the United States which are not due or callable for at least 4 years. This has been advantageous to the trust funds, historically, because long-term Federal obligations have had a higher rate of return than short-term obligations.

Trust fund investment earnings experience has, in fact, compared favorably with the average rate of return earned by prudent, well-established private investment organizations holding long-term securities, such as U.S. life insurance companies. For example, the net rate of return on investments—before Federal income taxes—for all U.S. life insurance companies was 8 percent in calendar year 1980 and 8.6 percent in calendar year 1981, according to the American Council of Life Insurance. The preliminary estimate for 1982 is 9 percent.

In comparison, the combined OASI and DI trust funds had a rate of return of 8.4 percent and 9.2 percent during the 12-month periods ending June 30, 1980, and June 30, 1981, respectively. The rate for the period ending June 30, 1982, was 10.3 percent.

I know there has been a lot of demagoguery on this issue on both sides of the Hill and among some representatives of the press. I think that investment strategy record speaks for itself, but I do think that it would be good for the committee and the Congress as a whole to clarify exactly how those funds should be invested.

Although investment income represented only 2.1 percent of total income to the trust funds in calendar year 1981, the management of trust fund assets will become increasingly important to the financial health of social security after necessary reforms are made and the trust funds are able to rebuild sufficient reserves to protect the system from temporary economic downturns.

We think it is important for the American people to know that the Congress has taken a look at the investment strategy and it has agreed on the best strategy for the Nation and the people we serve.

Since the National Commission on Social Security Reform is reviewing trust fund investment policies, it would be premature for the administration to recommend any specific changes in current investment policy until the Commission has issued its report and given the Congress the time to examine the issue.

Section 104 of the bill would increase the interest rate charged States on late payment of social security taxes to the rate imposed by the Internal Revenue Code on private employers. The code rate is based on the prime lending rate and is adjusted semiannually. It is now 20 percent and will be 16 percent for the first 6 months of 1983.

As you know, States are now charged 6-percent annual interest if they pay their contributions late. This rate—which is mandated by the Social Security Act—is far less than the rate imposed on private employers. Also, the trust funds are disadvantaged by the late payment of State taxes because the 6-percent rate is lower than the amount which could be earned if the taxes had been received on time and invested.

We support the intent of section 104 because the trust funds should not be disadvantaged by failure of States to pay social security taxes promptly. In June 1982, the HHS Inspector General recommended the same interest rate proposal that is included in the committee's bill.

There are, however, other approaches which the committee may want to take, especially in light of the fiscal status of some of the States. For example, one possibility is to use the rate of interest earned by new special obligations issued to the trust funds. The November interest rate on special obligations was 10⅝ percent. State social security taxes are credited to the trust funds only when actually paid so the trust funds lose investment interest when State taxes are paid late.

Thus, a rate based on new special obligations would place the trust funds in substantially the same position they would have been in if the States had made their deposits on time. In contrast, since private sector social security taxes are credited to the trust funds by Treasury when owed, the trust funds suffer no loss in the case of late payments.

Another option is a rate based on the average auction yield of 91-day Treasury bills. This option would tie the interest rate to the general fund's short-term borrowing costs. For the November 29 auction of 13-week Treasury bills, the average yield was 8.57 percent.

Title II of the bill would eliminate gender-based distinctions in the social security statute. Elimination of gender-based distinctions in the Social Security Act is long overdue. In 1977 this committee addressed this same issue in legislation that was passed by the House but dropped in conference.

This administration has attached great importance to dealing with sex-discrimination issues. President Reagan has established a President's Task Force on Legal Equity for Women which, along with OMB, is taking a hard look at possible areas of discrimination in the law.

A preliminary assessment indicates that the elimination of gender-based distinctions such as those at issue in this bill would probably have a negligible effect on the cost of the social security program. Part of the reason for the negligible cost effect is that many of the changes proposed in title II of the bill have already been implemented de facto as a result of court decisions.

However, legislation in this area is still necessary because some gender-based distinctions remain in effect and because there are ambiguities that necessarily result when court decisions are implemented without the accompanying statutory clarifications.

Let me now turn to title III of the bill, which concerns social security coverage. Section 301 is intended to improve the social security protection of U.S. citizens working outside the United States. Under present law, services performed by U.S. citizens working outside the United States for a foreign subsidiary of an American employer can be covered under social security at the option of the employer.

However, both the employer and the foreign subsidiary have to be corporations and the parent company must have a specified degree of control over the subsidiary in order for coverage to be provided.

At present, some U.S. citizens who are asked by their employers to work for affiliated businesses in foreign countries do not get social security credit for their work outside the United States because the explicit conditions in the law are not met. Section 301 would permit social security coverage to be extended to U.S. citizens working outside the United States if the parent employer is a sole proprietorship or a partnership.

In addition, the bill would reduce the percentage of interest of the parent company in the affiliate required for coverage. Section 301 would permit additional employees working for a foreign subsidiary of an American firm to continue to build social security protection.

Section 302 of the bill would correct an incongruity in the Social Security Act and Internal Revenue Code with respect to international social security agreements. Neither law specifies that earnings intended to be covered under social security as a result of international agreements are wages or self-employment for social security coverage and tax purposes.

Therefore, certain earnings that are intended to be covered under the U.S. system pursuant to an international agreement are not covered because U.S. social security taxes cannot be imposed on the earnings. Section 302 would remedy this situation by authorizing collection of social security taxes in these cases.

Sections 303 and 306 would make technical corrections to provide consistent treatment of certain foreign earned income and employer payments into simplified employer pension plans, respectively, for social security tax and coverage purposes.

Section 307 of the bill concerns the social security coverage status of certain public employee groups in Utah. The provision would simply assure that the social security treatment of certain entities in Utah would not change if the entities' names were changed. Your own staff materials on this anomaly reflect very well the idiocy of the situation we are in with respect to the Utah entities.

Sections 304 and 305 would cover under social security certain deferred compensation and standby pay, respectively. We do not now have enough information to evaluate the implications of these proposed changes.

Finally, let me turn to title IV which addresses nine miscellaneous technical issues. Most of these provisions are quite technical and would have insignificant effects on the social security trust funds. I will mention just a few of them.

Section 402 would change the effective date of the merger of the social security systems of the United States and the Northern Mariana Islands.

Under present law, the U.S. social security system will become applicable to the Northern Mariana Islands upon termination of the U.S. trusteeship of the Trust Territory of the Pacific Islands, or at an earlier date if agreed to by both governments. When the two systems are merged, the funds and the credits earned under the Northern Mariana Islands system will be tranferred to the U.S. social security system.

A problem arises because it is likely that the termination of the trusteeship, and hence merger of the two social security systems, will not occur on the first day of a calendar year. This would cause significant technical and administrative difficulties for both systems because certain changes—such as in the contribution and benefit base, the tax rate, the measure of quarters of coverage, and the exempt amounts under the earnings test—would be difficult to accomplish if merger did not occur on the first day of a calendar year.

Section 402 would provide that the merger would occur on the first day of the year following termination of the U.S. trusteeship.

The process of terminating the trusteeship is moving toward completion and could occur as early as fiscal year 1984, and section 402, if enacted, would avoid unintended complications.

Section 405 would correct an anomaly in the requirements for disability benefits for workers who had been entitled to disability benefits before age 31, recovered, and then became disabled again at age 31 or later. Under present law, a worker disabled before age 31 has to have quarters of coverage in only half of the calendar quarters ending with the quarter of disability.

In contrast, a worker disabled at age 31 or later must have 20 quarters of coverage during the 40-quarter period ending with the calendar quarter in which disability began. This last rule prevents some workers from becoming entitled to disability benefits if they originally qualified under the less strict rules for workers under age 31, recovered, and then became disabled again without having enough time to work long enough to earn 20 quarters of coverage before the second disability began. Section 405 would, in effect, extend the special rule for workers under age 31 beyond age 31 in these cases.

The problem with current law was dramatically brought to my attention and to the committee's attention in the case of a 33-year-old disabled Vietnam veteran who had two prior periods of disability—both established before he was age 31 and both ended because he returned to work. Despite having both legs amputated, this young man has tried repeatedly to work and become self-sufficient.

He is now over age 31, but because he has not had sufficient time to earn the 20 quarters of coverage needed by workers who are disabled at age 31 or later, he cannot again be entitled to disability benefits. This problem—which is also a work disincentive—would be corrected by section 405.

Section 408 is, we think, something more than a technical amendment because it has a cost and makes a policy change. Under current law, the payment of retroactive benefits is prohibited if the retroactive payments would require the lowering of future benefits.

One result of this provision of law is that, in some cases, a woman whose husband dies towards the end of a month may not receive a widow's benefit for the month of death unless she is able to file an application before the end of the month. Section 408 is intended to remedy that situation. However, the provision would have additional costs of $12 million in the first year. The change would also have the effect of allowing widows to receive retroactive reduced benefits which would make an exception to the provision adopted by Congress in 1977 which eliminated retroactivity for many beneficiary groups where permanently reduced benefits would result.

In conclusion, let me reiterate that we appreciate this committee's attention to resolving a number of troublesome technical problems with the current social security program.

I look forward to working with your committee on an effective legislative package to improve the operation of the social security program. I will be glad to respond to questions you may have.

Chairman PICKLE. Thank you, Mr. Deputy. First, I would want to ask as a matter of general position that you indicate to this committee the position of the SSA in all of these matters which you have mentioned. I noticed in a few instances you commented on them, but you did not say whether you would support them or are opposed to them.

One was a financing question. You felt it might be premature if the committee were to act in advance of the National Commission on Social Security Reform's consideration of this, depending on what time they might submit them. I would like to know if you are either for or against all of these, or if you have any objection.

For instance, in your discussion of section 408 which would allow retroactive benefits to a woman whose husband died at the end of a month, you indicate that that would cost $12 million. You did not say that you are against it. I assume from that that you just make that observation, but do not make an objection to it.

Mr. SIMMONS. The only problem we would have with this bill would be if the National Commission comes out with something, say, on investment strategy, which we like better than whatever is in the bill. Or if Treasury has a major problem with it, we would defer to them on the financing amendments.

We only point out that we are quite impressed with the way the investment policy has gone in the past, and I think the record speaks for itself.

On the rest of these, I would not take a strong position against any. As a matter of fact, most we would strongly support.

Chairman PICKLE. Also, in each of these sections, when you present your positions on them to this committee, will you indicate the costs or the revenue that might be involved?

Mr. SIMMONS. Yes, sir. We are sending a complete breakout on each of the amendments by our actuaries.

Some of them we can't even estimate, because they are very, very minor, but we will do the best we can to give you a bottom line on the bill.

Chairman PICKLE. I have another question for you.

Later on this afternoon, we are going to hear testimony from the National Senior Citizens Law Center group, and I think that testimony will probably center on section 209, dealing with the treatment of self-employed income in community property States.

In light of this testimony which we anticipate, because we have seen the advance copy, would you explain SSA's current administrative situation concerning the treatment of self-employed income in community property States? How do you handle it now?

Mr. SIMMONS. The way it happens now, the act provides that in community property States, all income from a business owned or operated by a married couple is deemed to be the husband's, unless the wife exercises substantially all of the management and control of the business.

As you might imagine, in some businesses it is difficult to say where one's effort begins and where the effort of the other party to the marriage leaves off.

The law regarding treatment in community property States has been held to be unconstitutional in several court cases. As a result, we are now forced to treat self-employment income of a married couple in a community property State the same as this kind of income in a noncommunity property State.

In the Edwards case just decided in 1982, the court ruled that self-employment income should be divided between the spouses, based on the amount of labor contributed by each.

To do that, of course, we have to go back and reconstruct records that may not be there, or make a best guess at what was the case.

The court also ruled that if dividing the earnings would be disadvantageous to a wife, she could elect not to have the earnings divided. This decision could require the reallocation of self-employment income for periods far in the past.

It could increase program costs because it would permit wives to choose the most advantageous of two ways of crediting such income, and use the same income to establish insured status and benefit amounts for both spouses.

Section 209, as it is in the bill now, would change the statute to conform to SSA's current practice, which is based on a number of court decisions. It would also provide authority for not following the undesirable ruling in the Edwards case. It would not address other situations in which wives who participate in family businesses do not get credit for their earnings.

I can ask Mary Ross to elaborate on this and what our current practice is, if that would be helpful to the committee.

Chairman PICKLE. Will you identify the people who are at the witness table?

Mr. SIMMONS. Yes. Mary Ross is Director of our Legislative Reference Office, and Louis Enoff is my deputy, deputy to the Deputy Commissioner.

Chairman PICKLE. Glad to have both of you.

Miss Ross, would you like to comment?

Ms. ROSS. I think that is reasonably covered. If we do need more detail on current practices, Lucia Swanson of——

Chairman PICKLE. Would you speak into the microphone? Put it a little closer to you.

Ms. ROSS. Lucia Swanson, who specializes in this, among other areas, might respond.

Ms. SWANSON. I am Lucia Swanson, Deputy Chief of the Coverage Branch in the Office of Legislative and Regulatory Policy.

What we do now with respect to self-employment income in community property States is the result of the first three court cases determining that present law is unconstitutional.

We now treat income in community property States the same as we do in noncommunity property States. That is, where a husband and wife carry on a business, and it is not a partnership, we allocate all the income to the spouse who is carrying on the business.

Now, this is different than the old rule, because, under the old rule, in order for the wife to acquire any earnings to her record, she had to be exercising substantially all management and control of the business. She had a tremendous burden of proof in order to acquire any credit for earnings.

Chairman PICKLE. The *Edwards* case is pending before the courts now. Can you give us some indication when that case might be adjudicated?

Ms. SWANSON. Right now, I believe that there is a jurisdictional issue that is being adjudicated in the Supreme Court. I am not up on exactly what the situation is with that case. I can find out for you.

[The following was subsequently received:]

Under *Edwards* v. *Schweiker,* a class action suit, self-employment income in community property States would be divided between spouses on a coproprietorship theory based on the amount of labor contributed to the business by each spouse. However, the court ruled that husbands who were receiving social security benefits at the time of the decision would not have their benefits reduced. Further, if dividing the earnings would be disadvantageous to a wife, she could elect not to have the earnings divided. The court also ordered the Secretary of Health and Human Services to send notices to class members concerning their rights under the *Edwards* case. In March 1982 notices were sent to all social security beneficiaries; at the end of October, notices were also sent to women in community property States whose claims for benefits were denied in August 1979 or later because of lack of insured status. The Social Security Administration is currently developing instructions to be used in making administrative determinations in conformity with the *Edwards* decision and expects them to be finalized by the end of January 1983.

The government did not oppose plaintiffs' contention in *Edwards* that section 211(a)(5)(A) of the Act was unconstitutional. Therefore, no appeal was filed on that issue. However, the Justice Department did file an appeal before the Court of Appeals for the ninth Circuit regarding the nature and scope of the relief granted plaintiffs. The appeal questioned the propriety of establishing a new standard for determining the allocation of self-employment income between spouses in community property States since the standard applied for distributing this income in other States was adequate to meet the constitutional defect in section 211(a)(5)(A). In addition, the appeal challenged the retroactive aspects of the relief granted and the mandate of the court that any reallocation of income between a husband and wife resulting from the court's order must not reduce the benefit of any current recipient. On July 27, 1982, the Court of Appeals for the Ninth Circuit dismissed the appeal for lack of jurisdiction finding that any decision holding a Federal law unconstitutional must be appealed directly to the Supreme Court. The dismissal was entered as a final judgment on August 19, 1982. The Justice Department is currently seeking review of the Ninth Circuit's dismissal of the appeal through a petition for certiorari filed in the Supreme Court. In the meantime, the Social Security Administration is continuing to take steps to implement the decision pending the results of the appeal.

Chairman PICKLE. It is difficult to ask the question, but what will happen, based on the *Edwards* case with reference to the legislation we have pending. As I understand what you are saying now, in community property States the income, according to your administrative handling now, is divided between husband and wife, or does it go to the man?

Ms. SWANSON. Right now, it goes to the spouse that is carrying on the business. Now, that depends on the facts in each case. It could be the wife or it could be the husband. This is in a situation where there is not a partnership.

Remember, if, in fact, there is a partnership, we can split the income in whatever proportion the partners may report.

Mr. SIMMONS. Under the *Edwards* case, I should point out the spouse was given a choice of which way to declare the income. If splitting the income would not be to the wife's advantage, then they would not have to split the income.

One of the problems with that is it gives both spouses eligibility based on the same earnings.

Chairman PICKLE. What we wish to do basically is to treat them all the same within the States. We would be interested in seeing what happens on this case, and why you apparently are handling it differently.

Ms. SWANSON. The way we handle it now is based on the first three court cases. Under *Edwards* we have notified the potential members of the class as to the decision. We have not fully implemented the *Edwards* case as yet.

*Edwards* decision there will be a different rule in community property States than there is in noncommunity property States again, because *Edwards* is a class action suit that applies only to community property States.

There is a larger issue here that has to do with the proper crediting of spouses' income in the case of businesses. It has to do with partnership splitting of income. It has to do with wives working for their husbands, but not receiving credit because as employees of spouses they are exempt from coverage under the Social Security Act.

This provision would conform the law to our practice under the remand decisions in the first three cases. The larger issue won't be addressed by *Edwards*. It is a substantive issue that needs to be addressed by the Congress, perhaps in a separate bill.

Chairman PICKLE. We are trying in this legislation to adopt a rule that we hope can be made applicable to all the States. That is the purpose of this legislation.

If you have any further comments with respect to the *Edwards* case, how you would want to handle it, we would like to hear from you before we get to any markup on this bill.

Mr. Deputy, before I get away from the subject as a whole, a couple of months ago we submitted to the SSA a question pertaining to the question of debt collection and some other matters.

It is very important as to how they are to be handled, and we wanted your views and positions on them. We haven't received those. Can you tell us why we haven't?

Mr. SIMMONS. You were supposed to have them Friday and we found a major mistake in one of the answers. You will have them this week. They are coming over right now. They are in the typewriter and they are on their way. We just had one big problem with one of them.

Chairman PICKLE. Mr. Gradison, do you have any questions?

Mr. GRADISON. Thank you, Mr. Chairman.

Mr. Simmons, this bill before us, so far as I know, includes some technical changes which the majority of the committee and the majority staff have prepared. I am sure at some stage of the game the minority on the subcommittee will have a chance to recommend some technical changes which it would like included, and I am going to bring those up in a minute.

I would like to ask you this question first. Have you been given an opportunity to suggest such technical changes as you feel, on behalf of the Social Security Administration, would be desirable to put in a technical title that might be part of a larger bill?

Mr. Simmons. Yes, we have, sir, and the agency has, as a matter of fact, gathered changes over a period of several months, even going back some years. Some of these are proposals which our own people have for a long time wanted to get in because they do simplify administration and do simplify the rules.

We have not been too actively pushing for any kinds of amendments this fall because, as you know, with all of the problems over financing and in light of the National Commission's deliberations, we didn't want to appear to be doing anything on social security because anything on social security becomes a major public issue.

We are glad to see this bill. We are glad to see almost all of the provisions in it, and we hope that the Congress will accept it. It addresses some of the more nettlesome problems in our administration of the law.

Mr. Gradison. Once the report of the Social Security Commission comes forward, and it is possible to get these issues out on the table for debate, would you anticipate that there might be additional technical corrections which you now know of that you would like to see but are not in a position to present to us at this time, or is everything in this title of a technical nature that you feel is required in the Social Security Act as they exist today?

Mr. Simmons. In a voluminous act I would never say, "this is everything that is wrong", but I do think this covers probably the lion's share of known technical problems that we have now.

If the Congress were to make some major changes in financing, taxing, et cetera, in the next year I am sure those will lead to a whole other set of 20 or 30 areas in the act that will have to be cleaned up with little technical amendments. Generally when we have something that is really threatening, is a real crisis situation in terms of management, we can usually get that resolved in some other bill percolating along, and that has always been the practice. But these are longstanding issues, some of them caused by court decisions, some just caused by anomalies in the law like the amendment on the age 31 cutoff for the young disabled worker. I don't think we have any other laundry list right now of anything that is more pressing than what is in this bill.

Mr. Gradison. Let me draw your attention to one issue which I feel should be a part of this bill, and ask your reaction to it, and that has to do with attempting to create a national death registry of some kind as a means of reducing, if not eliminating, the death fraud which exists.

As you may know, I introduced a bill, H.R. 5188, to deal with this. Subsequently, it was modified to incorporate suggestions, valuable suggestions which came from the Social Security Administration.

Would you support this new version with the modifications that the Social Security Administration has recommended?

Mr. Simmons. Yes, we do, very strongly. We are doing some experimental State death record matches now, as you know, and some of the things we are finding are disturbing to us. We do think that there has to be some national means of easy access to death records, without violating privacy and without starting some national "big brother" type thing. We do think that your bill, with the suggestions that we have made and with the good work of your staff, is a very desirable piece of legislation and we could support it.

Mr. GRADISON. Perhaps that could be part of this technical act that we are working on. It would seem to me so far as I know not to be controversial. However, there does seem to be some controversy, or at least question which has to be addressed, about this whole issue of privacy, and the workings of the Freedom of Information Act with regard to the data bank that might be created.

I realize that the Social Security Administration is dealing with a lot of matters which require privacy, frankly, which are of a lot more concern than whether a person is alive or dead, but which would be easily ascertainable, if it ever was necessary to probe into it with regard to some individual.

In other words, I think when you are keeping track of a person's earnings on a quarterly basis, that this would be something that would be of much more concern to most people than if it was known whether they were alive or dead. I think that is another question.

Aside from that, have you reached a decision whether you would prefer to maintain the death record data bank independently, or whether you would prefer that an independent group like the State registrars maintain the data bank and you have access to it.

Mr. ENOFF. We haven't reached a decision on that, but we feel that we are at a point that, between HHS and the State agencies, that the issue can be worked out.

Mr. GRADISON. How long would it take to reach a decision on this point? Do you think we might have it by the first of the year or the first of February?

Mr. ENOFF. Yes.

Mr. GRADISON. Before we begin marking up a bill?

Mr. ENOFF. It shouldn't take long. I think once the bill proceeds that we can sit down with those folks representing the States and they would be assured that their privacy interests are maintained.

Mr. GRADISON. I hope you will pursue that because, so far as I know, that is the only remaining technical question about that technical amendment, and it is an important question.

I don't mean to make light of it, but I think it ought to be possible to work it out.

One final point I would like to ask about——

Chairman PICKLE. Before the gentleman leaves that point, would you yield?

Mr. GRADISON. Of course, Mr. Chairman.

Chairman PICKLE. Do all States submit to the National Registry here the names of people who have died within the State and are buried? Is that information furnished by the States now nationally?

Mr. ENOFF. They furnish it, Mr. Chairman, but it is to the National Center for Health Statistics and it is used only for statistical purposes.

Chairman PICKLE. Is there any constitutional or legal question that we would have in gaining access to that information?

Mr. **Enoff**. Not in the way that Mr. Gradison's bill has been put forward, and with the proposed changes that we have stated, I don't think there is any question of constitutionality.

Chairman **Pickle**. Under the bill would we reimburse the State?

Mr. **Enoff**. Yes.

Mr. **Gradison**. My understanding, Mr. Chairman, is that the information is available and we are basically talking about another copy of tapes that already exist.

Mr. **Enoff**. Yes.

Mr. **Gradison**. I don't anticipate that there is going to be a heavy cost, but the legal issue is a very important one.

Mr. **Enoff**. Yes.

Mr. **Gradison**. With regard to these new records—their status under the Freedom of Information Act is really the question.

Mr. **Enoff**. I think that the thing that remains to be worked out is the logistics, and, as you know, we have our own set of computer problems that we are addressing in other ways. Originally, the bill would have had us go in the business of producing these tapes for others, and that is not our desire, but I don't think there is any constitutional issue that remains between the State agencies and ourselves.

Mr. **Gradison**. Mr. Chairman, there is one other issue which I personally think is of a technical nature and which I would like to raise at this time.

It has to do with the 90-session day requirement with respect to congressional review of totalization agreements that are worked out with other countries.

The way in which this is currently written, once agreement is reached with another country, it does not go into effect for 90 session days, which is defined to mean days that both the House and the Senate are in session.

Mr. Chairman, the way that has worked out in recent years is that in 1980 that period ran until July 25, in 1981 until September 14, and this year until August 10.

Mr. Chairman, I have no argument that there should be an opportunity for congressional review, none at all, nor am I arguing that 90 calendar days would be adequate especially because of the start-up times of a new Congress, but I would hope that the staff might review the idea of a version that might be 90 calendar days plus recesses or something like that.

It does seem to me an excessively long period of time to provide that agreement to sit here for 90 session days, which would have meant, for example, last year waiting until September 14 before agreement that was submitted January 1 could take effect.

I think that is really longer than is required to give appropriate opportunity for our review and oversight in these agreements. I raise this not so much to ask Mr. Simmons a question, because he could very properly say that is a congressional decision that has to do with how long Congress wants to review these things, but, Mr. Chairman, with the thought that this is of a highly technical nature, and might be difficult to pass on its own, it might be an appropriate and noncontroversial portion of the bill that we are working on.

Chairman PICKLE. Mr. Gradison, I suppose it would depend on what kind of agreement we might be able to work out within the committee and with the SSA. It is a vexing problem. It does seem like an inordinately long time if you must wait every day for the House and the Senate to be in session.

Mr. SIMMONS. Most of these treaties, now that we have some on the books, are very simple and very straightforward. We would have no problem with whatever review period the committee wanted or the Congress wanted.

Chairman PICKLE. I have never been one to want to rush into approving totalization agreements, and would have some hesitation to say we just go 90 calendar days, but we might be able to work out some kind of an approach, as Mr. Gradison has suggested.

I am not against considering it. I don't think we could consider it in this bill at this point, but it is something though to be cleared up and moved faster. I would agree with you on that.

Mr. GRADISON. I concur completely with your comment that 90 calendar days would not be adequate, Mr. Chairman. That is why I ask the consideration of 90 calendar days plus days that the House and Senate are both in recess, or something of the sort.

I think that would be better than what we have, and I would only ask that the staff examine that question and advise us before we mark up.

Chairman PICKLE. We will take under consideration "something of the sort."

Mr. GRADISON. Something short of it, if we leave it the way it is the world won't change a great deal, but it does seem to me if the two governments reach an agreement that we ought to find some way of reviewing it in less than 9 months.

Chairman PICKLE. We will consider that, Mr. Gradison.

Mr. Jacobs or any other members, are there questions of the Deputy Secretary?

Mr. GRADISON. If you have time for one more, this has to do with the interest issue and it may be that you want to defer to Treasury on this. I wonder whether the whole idea is sound of having a statutory calculation of interest payments that is based either on long-term maturities or short-term maturities or all maturities.

It seems to me that the maturity schedule that is appropriate to this trust fund depends upon the financial circumstances of the trust fund; that there have been times historically when the fund was flush with cash and anticipated having large reserves for an extended period of time when long-term issues might have been the appropriate financial holding.

Others, currently when we need the money or may need the money in a very short period of time, short-term holdings are the longest that would be prudent for this fund to be holding.

Therefore, I really wonder whether the trustee should not be able to designate a specific maturity date as any other trustee would do, and then see whatever the going rate is in the market for that maturity. For example, under one circumstance it might be 20 years, on another it might be 20 months.

I think it would enhance the discretion of the trustees, which doesn't bother me particularly, but also I think it would reduce a result which is appropriate to the maturity pattern that the fund may feel is desirable at any particular time.

I just wonder whether that alternative has been considered?

Mr. SIMMONS. I am sure Treasury will address that. Our main concern—when you said it could be 20 months or it could be 20 years—right now it looks like we need the rate, whatever it is, 20 minutes from now.

Mr. GRADISON. I understand that, and so today it would probably be equivalent to a 91-day bill.

Mr. SIMMONS. Right, but I do think the one concern we have—aside from the income to the trust funds, and not knowing how this works in the economy the way Treasury does—is, that, whatever formula is used, that the Congress adopt it in clear language that tells the taxpayers out there that they are getting the best deal for the dollars in those trust funds as is possible.

There have been a lot of myths about investments, a lot of demagoguery on the issue, such as: "They say banks can charge you 20 percent for mortgage money but the social security funds are only getting 8.9 percent." A lot of people get confused about that, and we would welcome the Congress clarifying investment policy once and for all, saying this is the best deal consonant with the needs of the Nation and of the people.

Mr. GRADISON. Thank you very much.

Chairman PICKLE. Thank you, Mr. Simmons and your group.

The next witness will be Mr. Carter of the Treasury, Mr. Warren Carter. Mr. C. Warren Carter, Deputy Assistant Secretary for Federal Finance.

Then we have Mr. Irvin E. Faunce, Deputy Commissioner, Bureau of Government Financial Operations.

If it makes no difference to you gentlemen, we will hear your testimony, Mr. Carter, and then we will proceed to Mr. Faunce.

## STATEMENT OF C. WARREN CARTER, DEPUTY ASSISTANT SECRETARY FOR FEDERAL FINANCE, DEPARTMENT OF THE TREASURY

Mr. CARTER. Mr. Chairman and members of the subcommittee, I am pleased to present the views of the Treasury Department on H.R. 7326, the Social Security Miscellaneous and Technical Improvements Act of 1982. My comments will be directed only at the investment provisions of section 103 of title I of the bill. The Treasury's Office of Tax Policy would like to present its views on the other titles of the bill at a later date.

At the outset, let me emphasize that decisions on the broader question of social security funding, that is, assuring adequate social security taxes or other sources of funds to meet future benefit payments, could affect investment policy.

On the other hand, investment earnings are only a minor source of income to the funds—1.3 percent of total receipts for the old-age fund in fiscal 1982. Thus, the funding problem obviously cannot be resolved by changes in investment policy.

The social security trust funds consist of four separate funds—the Old-Age and Survivors Insurance Trust Fund, the Disability Insurance Trust Fund, the Hospital Insurance Trust Fund, and the

Supplementary Medical Insurance Trust Fund. The assets of the funds were $38.1 billion as of November 30, 1982. The investment of the funds is by law the responsibility of the Secretary of the Treasury.

Under the social security laws, amounts in the social security trust funds not needed to meet current benefit payments and administrative expenses may be invested in interest-bearing obligations of the United States or in obligations guaranteed as to both principal and interest by the United States. The laws authorize the Secretary of the Treasury to issue special, nonmarketable public debt obligations to the trust funds and provide that the funds be invested in these special nonmarketable issues unless the public interest indicates otherwise. Under a 1960 amendment, these special obligations bear interest determined by a statutory formula which seeks to approximate the interest rates the Treasury would pay in the market for borrowing for a period of 4 or more years.

The law provides:

> Such obligations issued for purchase by the trust funds shall have maturities fixed with due regard for the needs of the trust funds and shall bear interest at a rate equal to the average market yield—computed by the managing trustee on the basis of market quotations as of the end of the calendar month next preceding the date of such issue—on all marketable interest-bearing obligations of the United States then forming a part of the public debt which are not due or callable until after the expiration of 4 years from the end of such calendar month * * *

Under this statutory interest formula, trust fund investments in special obligations made during the month of December 1982 bear interest at 10¾ percent.

The Treasury Department presented detailed testimony to your subcommittee on October 16, 1981, on policies and procedures governing the investment of the social security trust funds. I will direct my prepared comments today to the specific provisions of the bill you are now considering.

Section 103 of the bill would amend the existing statutory interest rate formula to provide that the trust funds be invested at the higher of two interest rates—the current rate based on market yields on Treasury obligations of 4 or more years to maturity, and a new short-term rate based on market yields on Treasury obligations with less than 4 years remaining to maturity. The explanatory material accompanying the bill indicates that the proposed amendment was prompted by the recent period of high short-term rates.

We believe that the long-range investment policies governing the social security trust funds, and other trust funds, should not be dictated by the happenstance of current relationships between short-term and long-term interest rates. At the time the present law governing the investment of the social security funds was enacted in 1960, long-term market rates were higher than short-term rates.

For example, 3-month Treasury bill yields were about 2.9 percent—coupon equivalent—and yields on 10-year Treasuries were about 4.1 percent. Thus, the statutory requirement that the interest rate on fund investments be based on market yields on Treasury securities with 4 or more years to maturity resulted in a higher return to the funds than would have been realized from a formula based on short-term rates.

Since 1960, long-term rates have generally been higher than short-term rates, but the relationship has fluctuated substantially with changing market conditions, and in recent years there have been prolonged periods when short-term rates were higher than long-term rates.

This relationship has changed dramatically over the past year, as short-term rates declined relative to long-term rates. The 3-month bill rate is currently about 8.6 percent—coupon equivalent—and the 10-year rate is about 10.7 percent. In comparison, in May 1981, the 3-month bill rate was as high as 18 percent, while the 10-year rate was 14.7 percent. Thus, the earnings of the funds will not necessarily be maximized by requiring that future investments be tied to either short-term or long-term rates.

In Treasury's testimony before the subcommittee on October 16, 1981, Deputy Assistant Secretary Stalnecker identified three deficiencies with the existing statutory formula for determining interest rates on social security trust fund investments:

First, the requirement that the interest rate be based on yields on Treasury marketable issues with 4 or more years to maturity prevents the Treasury from providing interest rates related to the specific maturities of the issues to the trust funds.

Thus, when short-term rates are higher than long-term rates, as was generally the case in 1979–81, the trust funds receive a lower rate of return than they would receive if the statute permitted Treasury to pay interest rates related to the yields on Treasury marketable issues of comparable maturities.

Second, the requirement that the obligations issued to the funds bear interest at a rate equal to the average market yield at the end of the month preceding the date of issue subjects the earnings of the funds to erratic fluctuations which may occur on any one day in the market, because of market reactions to short-term economic or financial developments or other unsettling news events.

A better approach would be to base the interest rate on an average over a period, which would provide a more equitable rate of return and would help assure more stability in the earnings of the funds.

Third, the requirement that the obligations issued to the funds bear interest rates equal to market yields on all marketable interest-bearing obligations of the United States of the prescribed maturities results in a somewhat lower rate of return to the funds than Treasury would be required to pay on new issues in the market. That is, under this statutory formula, Treasury must include in its rate computation the yields on many outstanding securities which were issued many years ago at market rates considerably below current market yields. Since such issues are thus traded at deep discounts in the current market, they are especially attractive to purchasers who benefit from the capital gains tax advantage of deep discount issues as well as to purchasers who gain special tax advantages from the so-called flower bonds which are redeemable at par for the payment of estate taxes. Consequently, such issues are traded at lower nominal yields than would be required on Treasury new issues.

This inequity to the trust funds could be remedied by permitting the Secretary of the Treasury greater discretion to base his rate determinations on current market yields on selected outstanding issues which are reasonably reflective of Treasury's current borrowing costs.

The two-tier interest rate setting system proposed in the bill would not deal with these three deficiencies in existing law and it would not provide sufficient flexibility to assure an equitable rate of return to the funds.

I am particularly concerned with the requirement in section 103 that the trust funds be invested only in short-term securities when short-term rates are higher than long-term rates, and vice versa. Such a policy would not necessarily benefit the funds in the long run, and such a policy would clearly not be consistent with prudent investment practices. For example, as indicated above, short-term interest rates are generally higher than long-term rates during periods when all interest rates are at cyclical highs. Thus a consistent policy of shunning long-term investments when short-term rates are higher than long-term rates would clearly be inadvisable and would not be followed by a prudent fund manager. As indicated above, we believe that the long range investment policies governing the social security trust funds and other trust funds should not be dictated by the happenstance of current relationships between short-term and long-term interest rates. There is no way of knowing whether any policy of maturity selection on the basis of interest rate forecasts will maximize fund earnings. We believe that the selection of maturities should be based on the expected cash needs of the funds and that the appropriate policy is to pick one strategy and stick to it.

Accordingly, a possible approach would be to consider the above alternatives to correct the deficiencies in the existing formula. While correction of these deficiencies in the statutory interest rate formula might not have a significant impact on the current earnings of the trust funds, there would be greater assurance of a more equitable and market-related return to the funds in the future.

I would note, however, that the National Commission on Social Security Reform is addressing this issue, and I am sure we will all want to consider their recommendations.

This completes my prepared remarks. I will be happy to answer any questions the subcommittee may have on the investment provisions of section 103 of H.R. 7326.

Chairman PICKLE. Thank you, sir.

I believe Mr. Faunce will now make a statement, Deputy Commissioner, Bureau of Government Financial Operations. Will you proceed?

## STATEMENT OF IRVING E. FAUNCE, JR., DEPUTY COMMISSIONER, BUREAU OF GOVERNMENT FINANCIAL OPERATIONS, DEPARTMENT OF THE TREASURY

Mr. FAUNCE. Mr. Chairman and members of the subcommittee, I am pleased to present the views of the Treasury Department on those sections of the Social Security Miscellaneous and Technical Improvements Act of 1982 concerning unnegotiated checks, check float, and interest on late payments of social security taxes by States.

Unnegotiated checks: Section 101 of the bill would require Treasury to credit social security trust funds with the amount of funds representing social security checks that have remained unnegotiated for at least 12 months.

The Treasury Department's position is that all classes of Government checks should be given equal treatment. Therefore, we are developing draft legislation that would limit the negotiability period of all Treasury checks and return unnegotiated amounts to Government accounts, including the social security trust funds.

Section 101 would also require Treasury to implement a system for distinguishing social security checks from other unnegotiated U.S. Treasury checks and transferring to the trust funds an amount equal to the value of social security checks unnegotiated for at least 12 months.

The Treasury's current accounting, reporting, and check payment and reconciliation system cannot identify unpaid checks by class. Therefore, any transfer of funds back to Government accounts under current system capabilities would be based on estimates.

Moreover, under the approach mentioned above of enacting legislation to limit the negotiability period for all Government checks, uncashed social security checks will, in fact, be transferred from the general fund of the Treasury to the Agency accounts.

I would note, however, that the National Commission for Social Security Reform is addressing this issue, and I am sure we will all want to consider their recommendations.

Float changes: Section 102 of the bill would require a study of the present float period, the time between check issuance and check payment, for benefits paid by check. Payments made by electronic funds transfer are charged to the trust funds on the actual due date, and no float is involved under this modern payment system encompassing about one-third of the social security payments.

Initially the Secretary of the Treasury would be required to report to the Congress and to the President on the results of the study and to issue regulations to adjust the float period, currently 2 business days, to reflect the actual lapse of time between check issuance and payment.

As you know, Federal agency accounting systems, Treasury's central accounting system, and the President's budget all record outlays on a checks issued basis.

Under the existing check processing system designed over 30 years ago, precise information on float for specific checks is not available.

While we receive summary data each day on the amount of checks charged to our account at the Federal Reserve, information on specific dates for specific checks is not available.

Attempting to identify the date the checks are paid using the Federal Reserve processing legends on the reverse of the checks involves more than a little guesswork due to the numerous bank and clearinghouse endorsements superimposed thereon.

The Inspector General of the Department of Health and Human Services recognized these difficulties in his report entitled "Float

Allowance Revisions Could Increase Interest Income to Trust Funds."

Our most recent study of check float, using the months of November 1981 and January 1982, indicates that 2 business days is still the norm. However, we review the float questions periodically to determine whether any adjustment to the present allowance is warranted.

The Department is, of course, vitally interested in assuring that the interests of both social security recipients and the taxpayers are protected.

In this connection, on April 23, 1982, the Secretary of the Treasury established an interagency task force consisting of representatives from the Social Security Administration, Railroad Retirement Board, Office of Personnel Management, Veterans' Administration, Department of Defense, and Office of Management and Budget, to explore greater utilization of electronic funds transfer in lieu of checks.

As part of this study, the issue of float is being examined further. Therefore, we do not believe that another joint study is necessary.

As a second thrust, the proposed legislation would require that the Secretary of the Treasury report on the feasibility of charging the trust funds for the actual amount of social security checks presented on a daily basis. Neither present nor planned changes in our check payment systems are designed to address this capability.

The modifications to accounting and check clearing operations would be inordinately complex and costly and cannot be justified in our present objectives for improving benefit delivery systems.

Our major focus will be on expanding the use of electronic funds transfer system. Under EFT, expenses presently charged to the trust funds for the cost of check preparation, mailing, processing, and claims will be substantially reduced and opportunities for fraud and abuse minimized.

We believe these efficiencies will, in their totality, outweigh any dollar gain to the trust funds resulting from float.

In our view, EFT will clearly be the delivery system of the future, and we urge you to support these efforts as opposed to costly systems to take advantage of float. The latter will only provide an incentive to capitalize on the inefficiencies of check processing when we should be moving away from labor-intensive, paper-based systems.

Interest on late State deposits: Under existing law, interest is charged on late payments of social security contributions due on the earnings of State and local government employees at an annual rate of 6 percent. The interest rate charged on late payments by private employers is based on the prime rate of interest charged by commercial banks.

Section 104 of the bill would amend existing law to provide this same prime rate basis for the late payments by State and local governments.

The prime rate formula proposed in the bill for the late deposit penalty may be inappropriate.

While use of this rate is justified for late tax payments by private employers, as an approximation of short-term alternative borrowing costs, State and local governments borrow at tax-exempt interest rates that are considerably lower than the prime rate.

In fact, State and local borrowing costs are generally lower than Treasury's borrowing costs. Nevertheless, the penalty rate should be high enough to cover the lost use of the funds to the Government and should thus be tied to Government's short-term borrowing costs.

It would be helpful if the rate chosen were readily available and easily understood, such as the 91-day T-bill average auction yield, which is published weekly in the financial press.

Accordingly, to provide an incentive for timely payment and to cover at least the Government's approximate cost of money, one reasonable approach would be charging the coupon equivalent of the average yield in the 91-day Treasury bill auction immediately preceding the due date of the State or local payment.

This completes my prepared remarks. I will be happy to answer any questions the subcommittee may have.

Chairman PICKLE. The Chair is going to ask for a recess for 10 or 15 minutes. We have a vote on the floor on the rule for the highway bill which comes out of this committee.

Members will need to go to the floor and vote so we will stand in recess for 10 minutes.

[Recess.]

Chairman PICKLE. The subcommittee will come to order.

I apologize to the witnesses but we have had a vote on the rule, and it was razor thin and we didn't know it until the last minute, so it took more time for the vote than normal.

I would first want to ask Commissioner Faunce a question regarding the unnegotiated checks, and I want to try to get down to the basics.

I know you propose a different way to handle this matter, and I don't know that I thoroughly understand each step that you are proposing. What we are concerned with in this committee is the money we want to see put into the trust fund, $300 million or more, perhaps some $30 million a year. These would represent the uncashed checks that would go back to the beginning of the program.

You talked about some kind of legislation that you would propose that would include reimbursing the trust fund for all past checks.

Does your draft include the reimbursement of all cash checks?

Mr. FAUNCE. Yes.

Chairman PICKLE. Uncashed checks?

Mr. FAUNCE. Yes, sir, from inception.

Chairman PICKLE. I can't hear you down there. Would you speak up?

Mr. FAUNCE. Yes, sir, our legislation would encompass all Government checks. We have some 5 million of them outstanding now over a year old, probably somewhere between $1 and $2 billion, so we are looking at the Governmentwide perspective for all Government checks.

Chairman PICKLE. The point I want to establish is that the draft that you would propose would reimburse the trust fund with this amount of money or whatever is involved?

Mr. FAUNCE. Yes, sir.

Chairman PICKLE. That is the main thing I want to get at. Do you object to us including in the provisions a new system in which you could identify social security checks in the legislation now before the committee?

Mr. FAUNCE. Yes, sir, we do. The legislation, as you have it, does not make the check nonnegotiable. The legislation that we are providing in the future will make the check nonnegotiable after some period of time.

There are 11 bills up here on the Hill now that are dealing with various periods of time anywhere between 90 days to 3 years for negotiability.

Chairman PICKLE. Mr. Carter, the National Commission this week or next week, I understand, may recommend some kind of a different approach according to the investment position of the social security fund. I don't know what that is. It is difficult for us to comment concerning something we don't know what is going to happen, if it does happen, but they may well do that. Do you know what they have talked about as a proposal, and would you agree with it?

Mr. CARTER. No, sir, I do not.

Chairman PICKLE. In both instances? The Commission is trying to find some way to find a better answer to the investment of the trust fund. During the past couple of years we have received a great deal of criticism from "experts" all across the country, some of them in Congress and many of them not, that we haven't invested our funds properly. And there was a hue and cry a year ago that we ought to drastically change our system.

What we are proposing really is a very modest sort of a change, giving us the option of both the short or long-term investments. But the salient part I got from you, Mr. Carter, was that in the overall measurements of our policy, that the right of return we receive on the social security trust fund is the rate of return basically on many of the long-term T-bills, almost the same. That we have not invested improperly.

Am I interpreting your statement correctly? Or do you think we have lost a great deal of money that should have been reimbursed in some other way?

Mr. CARTER. I am not quite sure I understand what you mean. I do not think we have lost money through imprudent investment practices. I could elaborate on the particular provision that you are asking for in this bill. The prudent investor would not put all of his eggs in one basket. Such a policy would expose his portfolio to great market risks. In fact, following such a policy as outlined in the bill would often lead to placing new investments at maturities at precisely the wrong time in the interest rate cycle.

As an example, using the interest rates in my testimony, those in May 1981, the portfolio manager using the proposed plan would have indeed received in 1981 an attractive 18 percent on his 3-month bills, versus 14.7 percent on 10-year notes. But in future months investments would have been rolled over at successively lower rates until later that year when long rates surpassed short rates. Had he invested a portion of his new investments in May

1981 in ten-year notes, he would have locked in nearly the highest rate ever attainable on Treasury securities.

A worse problem would be locking in potentially low long-term rates during those periods when the long rates were higher than short rates. During subsequent periods of prolonged increasingly higher rates, his long-term investments would suffer and his portfolio would perform poorly.

I might add one more point.

Looking at the problem another way, if one reasons that investment in the proposed manner is prudent or the best way, then the same should be true of borrowers. They would want to borrow short or long depending on the lowest rate available. For example, had the Treasury in its role of a debt manager followed this policy over the past few years, a substantial portion of Government debt would be outstanding for many years, again at extraordinarily high rates.

And one final note on this. One can certainly argue that the relatively attractive 10¾ percent combined return now being earned on the funds would not have been achieved had the Treasury ignored making investments in the long-term market when short rates were higher than long rates.

Chairman PICKLE. Mr. Carter, let me bring you back to a more specific question, then, because we are both ranging a bit now. Do you agree with the reservation that the Social Security Administration has expressed, that the system we propose in section 103 of the bill before us, that it would result in long-term lost money for the social security fund? Do you think what we have proposed would result in any long-term loss of any money?

Mr. CARTER. Any rate that you would receive would not result in a loss of money. But in the long run, the fund would probably not——

Chairman PICKLE. There would be loss of money for the social security system. That is what we are talking about.

Mr. CARTER. In following your plan, regardless of the rate that you invest at, whether it be 1 percent or 10 percent, you would earn that amount of money and there would be no loss of money to the fund. But you would——

Chairman PICKLE. We wouldn't have earned as much. I am talking about the difference between what we would earn under current law and a new proposal.

Mr. CARTER. But what you are doing here is speculating on interest rates, and you are potentially allowing for the fund to be receiving much lower rates of return than it could by following a more prudent pattern of investing a certain amount of funds in various maturity ranges.

Chairman PICKLE. We have a bit of trouble here understanding each other. The measure we have proposed here, recommended, that we take both a short term and long-term approach with a 4-year breakpoint, and make investments on that basis, we would have some option.

Do you oppose or do you favor that approach?

Mr. CARTER. I oppose that approach.

Chairman PICKLE. Would you tell me again why you would oppose it? Can you do it without going through all your testimony again?

What is your basic reason for it? Do you want to keep the present system?

Mr. CARTER. Well, I have proposed certain changes in my testimony.

Chairman PICKLE. Of the present system.

Mr. CARTER. Of the present system, exactly.

Chairman PICKLE. All right.

Mr. CARTER. Whereby we would obtain a market-based rate by maturity. In other words, at whatever maturity you placed new investments, you would receive that rate that would correspond to a current market rate. And this would result in a more equitable return to the trust funds over a long period of time.

Chairman PICKLE. Well, I can't seem to reach any general agreement with you. We have made this recommendation in the hopes that it might be a noncontroversial approach. We are not making major changes. We just simply are trying to distinguish between short- and long-term investments so we won't get caught in the long term which traditionally have been a good investment for us.

Overall it seems to me that the investment policy of the social security trust funds have been handled reasonably well. It is true, if you compare what has happened over the last 3 or 4 years with other proposals, it would appear we have lost money, or at least we won't have gained a lot of revenue that we could have. Yet when you consider the long term, the years as they would average out, it has been pretty prudent policy.

Now, the question is do we stay with what we have, perhaps with modifications you have recommended, or go with the approach we have suggested here? Do you think there is a big difference between the two proposals, what we have recommended and what you would change within the law? Would it mean a lot of money to the trust funds?

Mr. CARTER. Our proposals in the long run would make more money for the trust funds. There is no doubt in my mind about that.

Chairman PICKLE. Well, I need, then, to study your proposal more, Mr. Carter, which I will do. I may be submitting other questions to you because I need to have a better understanding of your proposal. I don't have a good, clear picture of it yet. At least we have your testimony in the record. We thank you for it.

Mr. CARTER. Thank you, sir.

Chairman PICKLE. I believe I have one other question. I believe this would go to Mr. Faunce.

Mr. Faunce, you are with the Government Financial Operations?

Mr. FAUNCE. That is correct, sir.

Chairman PICKLE. My question to you on this is on another subject, but I want to get it for the record. I am asking a question now on the matter of interfund borrowing for the social security system. It is my understanding that at the close of business tomorrow, on December 7, the Treasury Department as the managing trustee of the social security funds will borrow funds under the interfund borrowing authority in order to cover the OASI checks which went out on December 3. I assume that has to be the case; is that correct, that you are going to borrow funds?

Mr. FAUNCE. That's correct, sir.

Chairman PICKLE. How much is the current estimate that you will borrow tomorrow?

Mr. FAUNCE. Approximately $4.7 billion tomorrow afternoon.

Chairman PICKLE. $4.7?

Mr. FAUNCE. Yes, sir.

Chairman PICKLE. That compares to $600 million or thereabouts last month?

Mr. FAUNCE. Yes, sir. November 5 we borrowed $581 million.

Chairman PICKLE. Why is the sum so much larger this time compared to $600 million as to $4.7 billion?

Mr. FAUNCE. The last borrowing drew the social security trust funds down to basically a zero balance. Their income receipts during the month of November approximated $7 billion, plus the first few days of December. There are $12 billion worth of payments that will be going out, and the deficiency is, therefore, $5 billion. $4.7 billion precisely.

Chairman PICKLE. Will that money you are going to borrow come from the DI fund, or the HI fund or do you know?

Mr. FAUNCE. The money will be coming from the HI fund, hospital insurance, totally.

Chairman PICKLE. No checks come from the disability fund?

Mr. FAUNCE. The borrowing was from disability in November.

Chairman PICKLE. This time HI funds will provide the money, $4.7?

Mr. FAUNCE. Yes, sir.

Chairman PICKLE. Can you make an estimate what you think you will borrow at the end of this month?

Mr. FAUNCE. I do not have that vision to look at the end of this month at this time.

The 31st is the last day we can borrow. The amount of the money is still unknown.

Chairman PICKLE. We have borrowed, then, in November and December, a total of about——

Mr. FAUNCE. $5.3 billion.

Chairman PICKLE. About $5½ billion. Is that right?

Mr. FAUNCE. Yes, sir.

Chairman PICKLE. And if that is the case, then, it has been estimated you may have to borrow as much as $8 or $9 billion additionally. Is that a good estimate?

Mr. FAUNCE. That could very well be. The press release in November estimated that the total borrowing would be somewhere between $10 to $12 billion, that would be total for the whole year. It may be higher than that. But we do not know exactly what the number will be at this time.

Chairman PICKLE. Both in the interfund borrowing for tomorrow afternoon, and in the further borrowing that will occur on or before December 31, will you borrow as much as possible from the DI fund before you borrow from the HI fund?

Mr. FAUNCE. Our policy on borrowing has been to try to have an equal rate of return for the fund that we are borrowing from as what they will be losing on the funds provided to the social security fund.

To explain that more, the hospital insurance trust fund had to disinvest securities that approximated the same borrowing rate of interest that they would earn from the social security fund. Therefore, the rate was 10.75 percent for the month of December. We disinvested securities in HI that were equal to approximately 10.75 percent, so that they would still be earning that same rate. We would try to do that same thing at the end of the month on the borrowings, whether it be from disability or hospital.

Chairman PICKLE. I was going to ask you, what are the guidelines you use for determining whether you borrow from the HI or from the DI fund?

Mr. FAUNCE. The best guideline I could give you is you try to balance the funds so that the fund that will be disinvesting its securities would be disinvesting those securities at an approximate rate at what it would be earning on the borrowings from the social security funds.

Chairman PICKLE. What do you think will be the amount that will be borrowed from these, both, or a combination of these funds, by the end of the month?

Mr. FAUNCE. I do not have a number at this time, sir.

Chairman PICKLE. If we were to borrow, you borrowed 4.7 now from HI?

Mr. FAUNCE. Yes, sir.

Chairman PICKLE. And it is likely that you are going to borrow additionally from HI, or from DI, or a combination, is it not?

Mr. FAUNCE. That's correct. We will be borrowing an additional amount. It could be from both funds, or just one fund.

Chairman PICKLE. Do you think you could pay back those funds? What happens if you can't pay back the HI funds?

Mr. FAUNCE. The payment back would be predicated on the social security trust fund continuing in business. If the fund goes bankrupt, then it wouldn't pay it back. But I do not believe the Congress would allow the social security trust fund to go into that position, and not repay either of these funds. That would be speculative on my part, but I don't think you are going to do that.

Chairman PICKLE. Of course. I am not going to speak for the Congress, either. But it is a serious situation we face, because we know we have borrowed a considerable amount now, and chances are you are going to borrow out of necessity, because it has to carry you for another 6 months. You will borrow all you need; is that correct?

Mr. FAUNCE. That is correct. All we need.

Chairman PICKLE. And how much do you think that will be?

Mr. FAUNCE. Again, I do not have a number on that. It depends on the interest we will be earning. It will depend on the tax receipts primarily. What will be done by the Congress in terms of legislation it may pass to provide funding to the social security trust fund, other than through its normal current receipts.

Chairman PICKLE. We have heard figures up here, might be $8 or $9 billion, and it might be in that range.

Mr. FAUNCE. It could very well be, sir. But, again, the best figures we had was back in November where we said the total borrowing would be about $10 billion. It could exceed that.

Chairman PICKLE. I don't believe I will ask any further questions. You got higher than I was guessing. I want to stop at that point.

Mr. FAUNCE. Thank you, sir.

Chairman PICKLE. Thank you, gentlemen, very much, for your testimony.

Mr. FAUNCE. Thank you, sir.

Mr. CARTER. Thank you, sir.

Chairman PICKLE. I am going to ask that we combine the next witnesses in a panel. Eileen Sweeney, staff attorney for the Senior Citizens Law Center; Eldin H. Glanz, director of tax relations, Hercules, Inc., and Paul Jackson, consultant, National Small Business Association.

If you will, please come to the witness stand.

## STATEMENT OF EILEEN SWEENEY, STAFF ATTORNEY, NATIONAL SENIOR CITIZENS LAW CENTER

Ms. SWEENEY. Thank you, Mr. Chairman.

Chairman PICKLE. I am going to ask each of you to present your testimony. You may summarize if you wish. We will see that all of your statement appears in the record in its entirety. I will ask, then, Ms. Sweeney, if she would proceed first. Eileen Sweeney.

Ms. SWEENEY. My name is Eileen Sweeney. I am a staff attorney at the National Senior Citizens Law Center, and one of the attorneys representing the plaintiffs, in *Edwards* v. *Schweiker,* which challenged the constitutionality of section 211(a)(5)(A) of the Social Security Act.

I appear on behalf of Mrs. Mildred Edwards and the nationwide class of women which was certified in *Edwards,* to inform the subcommittee of the existence of the *Edwards* case, the court's order, and to recommend that, in light of *Edwards,* section 209 of H.R. 7326, entitled "Treatment of self-employment income in community property States" be deleted from the bill.

Title 42 United States Code section 411(a)(5)(A) provides that, in community property States, the husband will be credited with all the earnings from a business run by the husband and wife, unless the wife exercises substantially all the management and control of such trade or business, in which case all of such gross income and deductions shall be treated as the gross income and deductions of the wife.

Pursuant to section 209, that language would be replaced with a provision which gives all of the credit to the "spouse who is carrying on the trade or business." This would be effective for "taxable years that include the month of October 1980 or any subsequent month."

Section 411(a)(5)(A) was held to be gender discriminatory, in violation of the equal protection provision contained in the due process clause of the fifth amendment, in three cases where individuals sought review of the Secretary's application of the statute to their cases. The citations are included in my written statement at page 2.

The individual plaintiffs in these cases did not seek class certification. As a result, even though the courts held section 411(a)(5)(A) to be unconstitutional, SSA continued to apply the provision to women residing in community property States.

On October 20, 1980, Mildred Edwards filed suit on behalf of herself and all others similarly situated challenging the constitutionality of section 411(a)(5)(A) and seeking classwide relief from application of the provision.

The court certified a class of all applicants for or recipients of OASDI benefits on their own accounts as wage earners whose applications have been denied or for whom the monthly benefit amount has been reduced due to the omission from their earnings records of income earned while married and operating a trade or business in a community property State, as required by 42 U.S.C. section 411(a)(5)(A).

The *Edwards* court held that section 411(a)(5)(A) was unconstitutional and granted classwide relief which, in parts relevant to H.R. 7326, provides the following:

One, the Secretary will not apply the standard which he currently utilizes in noncommunity property States as that standard is not the one contemplated by 42 U.S.C. section 411(a).

Instead, "plaintiffs are entitled to an allocation of such coproprietor income between the spouses' earnings accounts * * * The basis for the division should be the relative amount of labor contributed by each.'

Two, the decision is to be applied retroactively, not just to income derived after October 1980.

A copy of the court's order is attached to my written statement.

Mr. Pickle, with regard to your question earlier about the status of the case the Government filed an appeal with the Ninth Circuit Court of Appeals from the ruling of the district court on unconstitutionality of the provision as well as relief provided.

The ninth circuit dismissed the appeal on the grounds that it should have been filed with the Supreme Court as the Secretary filed an appeal from the entire decision, including the unconstitutionality of the provision.

The Government, on November 24, 1982, filed a petition for certiorari with the Supreme Court on the issue of whether or not the ninth circuit should have dismissed their appeal. That is where the case stands at this point.

Chairman PICKLE. Thank you.

Ms. SWEENEY. While the stated purpose of H.R. 7326 with regard to the existing gender distinctions in the act is to conform the act to current practice which has resulted from earlier litigation, section 209 of the bill will gut the relief provided by the *Edwards* court to women injured by the unconstitutional provision.

In addition, section 209 is not justified by the longstanding case law interpreting the requirements of 42 U.S.C. section 411(a). In fact, the positions taken in section 209 are those put forth by SSA and rejected by the *Edwards* court.

First, section 209 will only apply the allegedly nondiscriminatory provision "with respect to taxable years that include the month of October 1980 or any subsequent month." This is exactly the language and the date rejected by the *Edwards* court. Unlike with most changes which affect benefits and for which imposition of an arbitrary effective date may be appropriate, the result of applying such an effective date to recalculations of earnings, such as here, is to perpetuate the unconstitutional discrimination for many years to come. The application of section 411(a)(5)(A) to any quarter of earnings in a woman's life will result in a lower benefit on her own account or the denial of benefits for less than adequate quarters.

Second, throughout the *Edwards* litigation, the Secretary has argued that, given the unconstitutionality of 42 U.S.C. section 411(a)(5)(A), he will apply the remainder of section 411(a) in community property States.

He interprets section 411(a) to require that, unless a partnership existed, all of the earnings will be credited to the spouse who exercised the greater management and control of the business. No division of earnings will be permitted.

In other words, despite the fact that both spouses worked, the Secretary would allow only one of them to receive credit for any of their earnings. Section 209 of the bill takes this position, which was rejected by the *Edwards* court.

While it is appropriate to apply the remainder of section 411(a), absent section 411(a)(5)(A), to community property jurisdictions, neither the statutory language nor the relevant case law support the limited interpretation which the Secretary proposed in *Edwards* and which is contained in section 209.

I would note specifically Mr. Simmons took the position the case law supports SSA. The *Edwards* court held that it did not, as have many courts which interpreted the provision prior to the *Edwards* court.

Applying the interpretation generally adopted by the courts, SSA should be required to analyze the self-employment income of each plaintiff and her spouse; based upon those findings, reallocate their earnings between them for purposes of adjusting their earnings records; and determine benefits based upon the revised earnings records.

The courts have generally held that section 411(a) applies to coproprietors as well as sole proprietors and partnerships. The *Edwards* court adopted the interpretation of the earlier decisions, rejecting the Secretary's narrow interpretation of the statute.

The courts addressing this issue have held that it is not necessary for an individual to be either a partner or a sole proprietor in order to be self-employed under section 411(a). Instead, they have held that the labor of the individual is the important factor, regardless of the label which may be applied to the particular business relationship. Therefore, the earnings derived from a coproprietorship qualify as self-employment income under section 411(a).

In conclusion, the case law in noncommunity property States and the *Edwards* order specifically addressing section 411(a)(5)(A) represent a legal framework very different from that set forth in section 209.

We recommend that, in light of the *Edwards* case, the subcommittee delete section 209 from the bill. Unlike the other litigation on gender-based distinctions, *Edwards* has not yet taken its full course.

At some point in the future, either when the *Edwards* order has been fully implemented or when the subcommittee is addressing a bill containing more controversial issues than those intended for

H.R. 7326, further subcommittee attention should be paid to this problem.

It should be noted that S. 3008, introduced by Senator Dole on October 1, 1982, includes many of the provisions included in title II of H.R. 7326. It does not include the amendments to section 411(a)(5)(A) set forth in section 209 of H.R. 7326.

Thank you for providing me with the opportunity to testify.

[The prepared statement follows:]

## STATEMENT OF EILEEN P. SWEENEY OF THE NATIONAL SENIOR CITIZENS LAW CENTER

### SUMMARY

1. Eileen P. Sweeney, a staff attorney at the National Senior Citizens Law Center, appears as one of the co-counsel for plaintiff in Edwards v. Schweiker, No. C-80-3959-MHP (N.D. Cal.), representing Mrs. Mildred Edwards and the nationwide plaintiff class certified by the district court.

2. Plaintiff in Edwards challenged the constitutionality of 42 U.S.C. §411(a)(5)(A), which requires that, in community property states, all income earned by a husband and wife operating a trade or business will be credited to the husband unless the wife can establish that she exercised "substantially all of the management and control of such trade or business." While three courts had earlier held the provision to be unconstitutional on behalf of individuals, SSA continued to apply the provision to other women.

The Edwards court certified a nationwide class of women injured by the provision who had received a decision from the Secretary on or after August 20, 1980.

3. The Edwards court held that §411(a)(5)(A) was unconstitutional and provided relief to the class. That relief includes a) retroactive application of the court's order to all years in which a woman's earnings were subjected to the provision; and (b) a requirement that the Secretary evaluate division of labor between the couple and allocate earnings accordingly.

4. §209 of H.R. 7326 guts the relief provided by the Edwards court both in terms of the standard to be applied and the effective date. Application of the October, 1980 effective date, which was sought by the Secretary in Edwards and rejected by the court, will perpetuate the discrimination set forth in §411(a)(5)(A) for many years to come.

5. Therefore, we recommend that §209 be deleted from H.R. 7326, and note that S. 3008, introduced by Senator Dole on October 1, 1982, does not include this provision among the gender distinctions to be addressed by legislation at this time.

My name is Eileen P. Sweeney. I am a staff attorney at the National Senior Citizens Law Center (NSCLC).

NSCLC is a national support center, specializing in the legal problems of elderly poor people. We are funded by the Legal Services Corporation and provide support services to legal services attorneys throughout the country with respect to the legal problems of their elderly clients.

I am one of the attorneys representing the plaintiffs in Edwards v. Schweiker, Civil Action No. C-80-3959 MHP (N.D. Cal.), which challenged the constitutionality of §211(a)(5)(A) of the Social Security Act. I appear on behalf of Mrs. Mildred Edwards and the nationwide class of women which was certified in Edwards to inform the Subcommittee of the existence of the Edwards case, the court's order, and the current status of the case, and to recommend that, in light of Edwards, §209 of H.R. 7326, entitled "Treatment of self-employment income in community property states" be deleted from the bill.

## I. EDWARDS v. SCHWEIKER

42 U.S.C. §411(a)(5)(A), §211(a)(5)(A) of the Social Security Act, provides that, in community property states,*

> "... all of the gross income and deductions attributable to such trade or business shall be treated as the gross income and deductions of the husband unless the wife exercises substantially all the management and control of such trade or business, in which case all of such gross income and deductions shall be treated as the gross income and deductions of the wife."

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* The states which currently have community property laws are Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas and Washington. Puerto Rico is also a community property jurisdiction.

This provision was held to be gender discriminatory, in violation of the equal protection of the Due Process Clause of the Fifth Amendment, in three cases where individuals sought review of the Secretary's application of the statute to their cases. See Carrasco v. Secretary of Health, Education and Welfare, 628 F.2d 624 (1st Cir. 1980); Hester v. Harris, 631 F.2d 53 (5th Cir. 1980); Becker v. Harris, 493 F.Supp. 991 (E.D. Cal. 1980).

The individual plaintiffs in these cases did not seek class certification. As a result, even though the courts held §411(a)(5)(A) to be unconstitutional, the Social Security Administration continued to apply §411(a)(5)(A) to women residing in community property states. On October 20, 1980, Mildred M. Edwards filed suit on behalf of herself and all others similarly situated against Richard S. Schweiker, Secretary of the Department of Health and Human Services. Plaintiffs challenged the constitutionality of 42 U.S.C. §411(a)(5)(A) and sought class-wide relief from application of the provision.

The court certified the following class, pursuant to Federal Rules of Civil Procedure 23(a) and (b)(2):

> All applicants for or recipients of Old Age, Survivors and Disability Insurance benefits, 42 U.S.C. §401 et seq. on their own accounts as wage earners whose applications have been denied or for whom the monthly benefit amount has been reduced due to the omission from their earnings records of income earned while married and operating a trade or business in a community property state, as required by 42 U.S.C. §411(a)(5)(A).*

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* "Order Granting Plaintiffs' Motion for Summary Judgment as to Liability and Class Certification and Denying Defendant's Motion for Remand" (May 22, 1981, ¶ 3) In a later order, the court limited the class to individuals who received a "final decision" from the Secretary no earlier than 60 days prior to the filing of this action. ("Order," August 14, 1981, as amended, August 20, 1981)

On May 22, 1981, the Edwards court held that §411(a)(5)(A) was unconstitutional.*

After lengthy negotiations between the parties regarding class relief were not productive, the court issued an order regarding class relief which, in parts relevant to H.R. 7326, provides the following (a copy of the decision is attached):

> 1. The Secretary will not apply the standard currently utilized in non-community property states to these cases as that standard is not the one contemplated by 42 U.S.C. §411(a). See Rasmussen v. Gardner, 374 F.2d 589, 594 (10th Cir. 1967). Instead, "plaintiffs are entitled to an allocation of such co-proprietor income between the spouses' earnings accounts ... The basis for the division should be the relative amount of labor contributed by each."
>
> 2. The decision is to be applied retroactively, not just to income derived after October 1980. "[P]laintiff class members are entitled to a recomputation of their earnings records, extending back to the beginning of Social Security, if necessary."
>
> 3. Plaintiffs will be permitted to correct incorrect income entries in their SSA records, pursuant to the exemption of §405(c)(5)(G). Further, even if that exemption was not available, SSA can not apply the three year, three months, and fifteen day rule [42 U.S.C. §405(c)(4)] in these cases.

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* "Order Granting Plaintiffs' Motion for Summary Judgment as to Liability and Class Certification and Denying Defendant's Motion [illegible] Remand," (May 22, 1981, ¶1, 2)

To this day, neither Mrs. Edwards nor any member of the class has had their case readjudicated by the Secretary under a constitutional standard.*

## II. *§209 of H.R. 7326*

While the stated purpose of H.R. 7326 with regard to the existing gender distinctions in the Act is to conform the Act to current practice which has resulted from earlier litigation, §209 of the bill will gut the relief provided by the *Edwards* court to women injured by the unconstitutional provision. In addition, §209 is not justified by the long-standing case law interpretting the requirements of 42 U.S.C. §411(a).

The positions taken in §209 have been rejected by the *Edwards* court.

a. *Retroactivity*: §209 will only apply the allegedly non-discriminatory provision "with respect to taxable years that include the month of October 1980 or any subsequent month."

This is exactly the language and the date rejected by the *Edwards* court. Unlike with most changes which affect benefits and for which imposition of an arbitrary effective date may be appropriate, the result of applying such an effective date to recalculations of earnings, such as here, is to perpetuate the unconstitutional discrimination for many years to come. For example, hypothetical Mrs. A just recently became 65 years old. While she has not worked in the past few years due to poor health, she did work for a number of years between 1955 and 1975. During those years, she and her husband jointly operated a business in California. Just before her 65th birthday, in June, 1981, Mrs. A applied for Social Security benefits on her own account. Her application will be denied on the basis of 42 U.S.C. §411(a)(5)(A), if the 1980 effective date is utilized. Because of Mrs. A's earnings were earned prior to 1980, she remains totally subjected to §411(a)(5)(A).

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* The defendant filed a motion for a stay pending appeal with the district court which was denied. The Secretary then filed a notice of appeal from the final judgment of the court, which had granted plaintiffs' motion for summary judgment, in the Ninth Circuit Court of Appeals. That appeal was dismissed for lack of jurisdiction, citing *Donovan v. Richland County Association for Retarded Citizens*, 102 S.Ct. 713 (1982). (Order of July 27, 1982, filed August 19, 1982) The Secretary filed a petition for a writ of certiorari in the Supreme Court on November 24, 1982, seeking review of the Ninth Circuit's dismissal of the appeal.

A similar problem will exist where some portion of the female wage earner's earnings record was completed prior to the taxable year which includes October 1, 1980. For example, Mrs. B and her husband have jointly operated a business in Idaho since 1975. She expects to retire at age 65 in 1984. At that point, if §411(a)(5)(A) is not applied to any of her earnings, she will have sufficient quarters of credit to enable her to receive benefits on her own account. However, if the 1980 effective date is imposed, Mrs. B will not be eligible for benefits on her own account. Further, even if a person such as Mrs. B had a few quarters of earnings recorded from an earlier period in her life, the application of §411(a)(5)(A) to any quarter of earnings in her life will result in a lower benefit amount on her own account. Therefore, even though she might be found entitled to receive benefits, the amount of her benefits will be lower than she would receive if all of her earnings were counted.

b. The standard: Throughout the Edwards litigation, the Secretary has argued that, given the unconstitutionality of 42 U.S.C. §411(a)(5)(A), he will apply the remainder of §411(a) in community property states. He interprets §411(a) to require that, unless a partnership existed, all of the earnings will be credited to the spouse who exercised the greater management and control of the business. No division of earnings will be permitted. In other words, despite the fact that both spouses worked, the Secretary would allow only one of them to receive credit for any of their earnings. §209 of the bill takes this position, which was rejected by the Edwards court.

While it is appropriate to apply the remainder of §411(a), absent §411(a)(5)(A), to community property jurisdictions, neither the statutory language nor the relevant case law support the limited interpretation which the Secretary proposed in Edwards and which is contained in §209. Applying the interpretation generally adopted by the courts, SSA should be required to analyze the self-employment income of each plaintiff and her spouse; based upon those findings, re-allocate their earnings between them for purposes of adjusting their earnings records; and determine benefits based upon the revised earnings records.

42 U.S.C. §411(a) provides, in relevant part:

> (a) Net earnings from self-employment. The term 'net earnings from self-employment' means the gross income, as computed under chapter 1 of the Internal Revenue Code [of 1939], derived by an individual from any trade or business carried on by such individual, less the deductions allowed under such chapter which are attributable to such trade or business, plus his distributive share (whether or not distributed) of the ordinary net income or loss, as computed under section 183 of such code [of 1939], from any trade or business carried on by a partnership of which he is a member . . . .

The courts have generally held that this language applies to co-proprietors as well as sole proprietors and partnerships. The Edwards court adopted the interpretation of the earlier decisions, rejecting the Secretary's narrow interpretation of the statute.

The courts addressing this issue have held that it is not necessary for an individual to be either a partner or a sole proprietor in order to be "self-employed" under §411(a). Instead, they have held that the labor of the individual is the important factor, regardless of the label which may be applied to the particular business relationship. Therefore, the earnings derived from a coproprietorship qualify as self-employment income under §411(a). This approach is consistent with the ruling of the Ninth Circuit Court of Appeals, in Delno v. Celebrezze, 347 F.2d 159, 162 (9th Cir. 1956). In interpreting another portion of §411(a), the court specifically held that the provisions of §411(a) should be interpreted so as to favor coverage:

> The premise of the system established by Part II of the Act [Title II, the Old Age, Survivors, and Disability Insurance program] is that all gainfully employed persons are to be covered, except as specifically excluded. The language of the Act is therefore to be interpreted in favor of coverage. (Footnotes omitted.)

In Rasmussen v. Gardner, 374 F.2d 589 (10th Cir. 1967), the plaintiff filed a claim for benefits based on the earnings record of his deceased wife, seeking a lump sum death benefit and benefits for their three children. The claim was denied by the Secretary based upon a finding that the plaintiff's wife did not have insured status at the time of her death. The plaintiff claimed that his wife had acquired eight quarters of coverage from the earnings of a hotel which he and his wife owned and operated together. [These quarters of coverage would render her insured.] The administrative law judge found that both the plaintiff and his wife took an "active part in the operation of the hotel . . . either of them performed the duties when they were available and the necessity arose." 374 F.2d at 592. The plaintiff did not argue that he and his wife had entered into a formal partnership. Instead, he argued that he and his wife "individually earned self-employment income by participating in the operation of the hotel" and thus the earnings of the hotel should be equally divided between the two. 374 F.2d at 593. The ALJ rejected the claim, finding that a partnership did not exist and that there was no other basis for awarding benefits.

After the district court upheld the Secretary, the Tenth Circuit Court of Appeals reversed, finding "nothing in the language of §211(a) of the Act indicating that a partnership is the only basis upon which coproprietors of a business can each be credited with self-employment income for social security purposes" and concluding that the administrative interpretation of the statute was "too narrow," Id.:

> The facts in the record disclose that the [hotel owned by plaintiff and his wife] was owned and operated as a small-scale family enterprise by the appellant and his wife. Each of the participants was self-employed. There is also no requirement in the Act, nor indication in the legislative history (U.S. Code Cong. Service, 1950, pp. 3452-53), that the enterprise be a sole proprietorship. We hold that the existence of a partnership is not a necessary condition for dividing self employment income between coproprietors of the family enterprise here concerned, and the crediting of such income to their respective earnings accounts for social security purposes. 374 F.2d at 594 (emphasis added)

Further, citing Delno, supra, the court noted that "[t]he congressional policy underlying federal social security legislation requires the courts to interpret the Act liberally, and any doubts should be resolved in favor of coverage." Id.

Having found that Mrs. Rasmussen was entitled to quarters of credit, the court then turned to the issue of how to divide the earnings between the records of Mr. and Mrs. Rasmussen. Relying upon Mr. Rasmussen's testimony at the hearing that "he worked in the hotel as much as his wife did, and that both worked most of the time," the court concluded that this "would appear sufficient to equally divide the income under the other facts in the record." 374 F.2d at 495.*

Courts faced with co-proprietorship factual situations have either relied upon Rasmussen or adopted rationales for awarding benefits which are identical to or extremely similar to the Rasmussen holding.** In Dickmann v. Finch, 315 F.Supp. 1071

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* After the ruling in Rasmussen, the Secretary issued Social Security Ruling 68-48c in which he stated that he did "not acquiesce in the subject decision." "The Administration holds that in the absence of a finding that a business, jointly-owned by a husband and wife in the operation of which each performs services, is operated by the husband and wife in 'partnership' within the meaning of §211(a) and §211(d) of the Social Security Act, 42 U.S.C. §411(a) and 411(d), there is no basis in the Social Security Act for a determination that both the husband and wife are self-employed in the operation of the business." It should be noted that there is no statutory authority for issuance of such declarations of non-acquiescence.

** There is a line of cases which appears to support the §209 approach. In these cases, courts have held that the plaintiff had not established that a partnership existed and thus rejected the claim that quarters of credit should be credited. See, for example, Garrett v. Secretary of HEW, 397 F.Supp. 400 (W.D. Va. 1975); and Breashears v. Mathews, 440 F.Supp. 1230 (W.D. Ark. 1977). However, unlike the cases discussed in the text, it does not appear that the plaintiffs challenged the Secretary's interpretation of §411(a). Instead, they attempted unsuccessfully to

(E.D. Wis. 1969), the plaintiff and his wife had jointly owned and operated a tavern. After he retired, he transferred the business to his wife and she reported self-employment income. The Secretary ruled that the husband was subject to recovery of an overpayment of benefits, because the business was his, not his wife's, and the earnings should therefore be credited to his account. The court rejected this argument, finding Rasmussen applicable, and noting that "[t]he record does not reflect that plaintiff was the controlling manager, guiding light, or moving spirit of the enterprise to warrant attributing income derived from the labors of his wife to his earnings account." Id. at 1073.

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place their factual situations within the definitions imposed by the Secretary. In both cases cited, the courts rejected plaintiffs' arguments that a partnership existed relying upon a lack of documentary evidence of such an arrangement. 397 F.Supp. at 401, 440 F.Supp. at 1234. In Breashears, the plaintiff and her husband had purchased a gas station with their joint savings. She worked at the station full-time, took care of the books and business records, ordered supplies, and dealt with salespeople and customers. The court ruled that "Mrs. Breashears was only working in her capacity as a helpmate to her husband." 440 F.Supp. at 1234. Unfortunately, §209 would perpetuate this traditional view of the role of women which has been for many years reflected in SSA's treatment of women. For example, in Social Security Ruling 62-8 (1962), the husband operated a wholesale bowling supply business which was started in part with a loan from his wife. The wife originally kept the books, prepared invoices and took telephone orders. As the business grew, she worked full-time at the store while her husband spent his time out on sales visits. The Secretary held that the couple had not intended to conduct their business as a partnership, finding that they had not held themselves out to the public as a partnership, and that the business name, license and letterhead were in the husband's name. Further, the wife's contributions to the business were of the kind "ordinarily exercised by a wife who renders assistance to her husband in the operation of his business."

More recently, in Ballweg v. Califano, 469 F.Supp. 458 (D.Neb. 1979), the district court quoted from the Social Security Appeals Council's opinion in which was stated: "None of these affidavits shows that the claimant was performing any more than her spousal duties in helping her husband." Id. at 462.

A similar conclusion was reached in Freiburg v. Mathews, CCH Unempl. Ins. Rptr. ¶15,220 (S.D. Ill. 1977). There, the couple operated a tax accounting business. Although the plaintiff husband did the majority of work in the business during the early years of the marriage, by 1970 his wife was working an equal amount. In 1973, when a second office was opened, the plaintiff's wife took over the operation of the first office, performing the work for the clients and making the necessary business decisions. After upholding the Secretary's conclusions that neither a partnership nor a sole proprietorship existed, the court noted that "in order to be self-employed for purposes of the Social Security Act, it is not necessary that one be either a partner or a sole proprietor." The court held that where, as here, the wife "contributed substantial labor of the same character and nature as that of her husband" to the family enterprise, the relationship must be deemed self-employment for purposes of social security. "To hold otherwise," the court concluded, "would be to exalt form over substance."

In Raines v. Harris, 508 F.Supp. 17 (W.D. Va. 1980), the plaintiff filed an application for retirement benefits based on income earned in operating a 10-acre farm. During the two years in question, following her husband's third heart attack, the plaintiff performed the majority of the physical work on the farm, including planting the entire crop and tending it throughout the growing season. Her husband's sole contribution to the farm during this period was maintenance of the books, "such as they were," for the farming business. 508 F.Supp. at 19. Despite this arrangement, the Secretary denied the plaintiff's claim for benefits and concluded that the farm was primarily owned and operated by the plaintiff's husband.

On appeal, the district court reversed. While agreeing that neither a sole proprietorship nor a partnership existed, the court stated: "[I]n order to be self-employed for purposes of the Social Security Act, it is not necessary that one be either a partner or a sole proprietor." Id. Following the pattern of the decisions in Rasmussen, Dickmann and Freiburg, and citing those decisions, the court took note of decisions finding the labor of the individual to be the important factor, and of the Congressional policy requiring liberal interpretation of the Act, before holding that "at least for the years 1975 and 1976, Mrs. Raines contributed substantial labor" to the family farming enterprise. Id. Such a relationship, the court held, must be self-employment for purposes of determining quarters of coverage under the Social Security Act.

## Conclusion

The case law in non-community property states and the Edwards order specifically addressing §411(a)(5)(A) represent a legal framework very different from that set forth in §209. We recommend that, in light of the Edwards case, the Subcommittee delete §209 from the bill. Unlike the other litigation on gender-based distinctions, Edwards has not yet taken its full course. At some point in the future, either when the Edwards order has been fully implemented or when the Subcommittee is addressing a bill containing more controversial issues than those intended for H.R. 7326, further Subcommittee attention should be paid to this problem. It should be noted that S. 3008, introduced by Senator Dole on October 1, 1982 (Cong. Record

S 13303, daily ed. October 1, 1982), includes many of the provisions included in Title II of H.R. 7326. It does not include the amendments to §411(a)(5)(A) set forth in §209 of H.R. 7326.

Given the Edwards order, the result of passage of §209 would mean the loss of eligibility for benefits or substantial reductions in benefits for many women.

Thank you for providing me with the opportunity to testify.

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CLERK, U. S. DIST. COURT
SAN FRANCISCO

UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

MILDRED M. EDWARDS, individually and on behalf of all others similarly situated,

Plaintiffs,

vs.

RICHARD S. SCHWEIKER, Secretary of the Department of Health and Human Services,

Defendant.

No. C-80-3959

MEMORANDUM DECISION AND ORDER

Plaintiffs challenged the constitutionality of 42 U.S.C. § 411(a)(5)(A),[1] which governs the treatment of self-employment income in community property states. A class was certified of

> All applicants for or recipients of Old Age, Survivors and Disability Insurance benefits, 42 U.S.C. § 401 et seq., on their own accounts as wage earners whose applications have been denied or for whom the monthly benefit amount has been reduced due to the omission from their earnings records of income earned while married and operating a trade or business in a community property state, as required by 42 U.S.C. § 411(a)(5)(A).

The class was further limited to members who received a final decision from the Secretary of Health and Human Services within 60 days of the filing of the action.

Section 411(a)(5)(A) was found to violate the due process clause of the fifth amendment because it unlawfully discriminated against women on the basis of sex.[2] The issue now before the court is what relief is to be afforded class members who were adversely affected by the operation of the statute.

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SCOPE OF RELIEF

Defendant proposes to treat plaintiff class members as the agency now treats non-community property claimants.[3/] Under agency interpretation of § 411(a), self-employment income can be derived only from partnerships or sole proprietorships. If claimants cannot meet the partnership criteria, a determination is made as to which spouse is the sole proprietor. All income is then allocated to that spouse's account. Defendant argues that this is a sex-neutral standard.

The court finds this solution inappropriate. First, community property claimants differ significantly from other claimants in that each spouse owns fifty percent of the business property. This is likely to make the factual determination of who was sole proprietor much more difficult. A strong possibility exists that such a sex-neutral standard would result in practice in an unstated sexually discriminatory presumption. Second, the court is not persuaded by the agency interpretation of the statute. Section 411(a) discusses partnerships and individuals, not sole proprietorships. This does not preclude the possibility of co-proprietorship, where the business does not meet the partnership requirements but nevertheless employed both spouses. Rasmussen v. Gardner, 374 F.2d 589, 594 (10th Cir. 1967).

Plaintiffs are entitled to an allocation of such co-proprietor income between the spouses' earnings accounts. Such a resolution was suggested in Hester v. Harris, 631 F.2d 53, 56 (5th Cir. 1980). The basis for the division should be the relative amount of labor contributed by each. See Rasmussen v. Gardner, 374 F.2d at 594.

RETROACTIVITY

Defendant proposes that elimination of the presumption in favor of husbands under § 411(a)(5)(A) be applied only to income derived after October 1980. This is when the decision to acquiesce in Becker v. Harris, 493 F.Supp. 991 (E.D. Cal. 1980), became final. Plaintiffs object, arguing that such a limit essentially nullifies any relief.

Retroactive application of a judicial decision is the norm. "The concept stems from the Blackstonian view, that judges do not make law; they find law. Judicial declaration of law is merely a statement of what the law has always been." Cash v. Califano, 621 F.2d 626, 628 (4th Cir. 1980). Nevertheless, in recognition that retroactivity sometimes causes inequities, the Supreme Court developed a test for determining when prospective-only application is appropriate. Chevron Oil Co. v. Huson, 404 U.S. 97 (1971). "However, Huson considers the retroactive effect of a separate decision, rather than the scope of relief to be afforded in the case before a court." Shannon v. United States Civil Service Commission, 444 F.Supp. 354, 369 (N.D. Cal. 1977), modified on other grounds, 621 F.2d 1030 (9th Cir. 1980). Like Shannon, this case involves the relief to be afforded the plaintiff class herein, since this court decided liability. Therefore, the Huson factors need not be applied in determining that relief should be retroactive beyond the October 1980 date.

Even if the Huson test is used, retroactivity is still appropriate. Huson provides a three-part test. First, the decision which is to be applied prospectively must establish a new principle of law, not "clearly foreshadowed" by earlier precedent. Second, prospective application must further the purpose of the rule. Third, the equities must weigh against retroactivity. Chevron Oil v. Huson, 404 U.S. at 106-07. All three prongs of the test must be satisfied for prospective only application, and the party arguing against retroactivity bears the burden of persuasion. See Cash v. Califano, 621 F.2d at 629.

The first factor weighs in favor of retroactivity. There was a substantial likelihood that § 411(a)(5)(A) would be struck down on gender discrimination grounds. Given the strong line of gender discrimination cases decided by the Supreme Court in the last decade,

> the most the Secretary could have hoped for was a halt in a very clear trend. None of the nonretroactivity cases have turned on so tenuous a proposition. Instead those cases have either involved a complete reversal of prior law, [citation omitted], or a pronouncement upon a case of first impression [citation omitted].

Cash v. Califano, 621 F.2d at 630. This case fits neither of those categories.

The second factor to be considered is whether prospective application would further the purpose of the rule. The Ninth Circuit has read § 411(a) to favor coverage. "The premise of the system . . . is that all gainfully employed persons are to be covered, except as specifically excluded." Delno v. Celebrezze, 347 F.2d 158, 162 (9th Cir. 1965) (footnote omitted). The purpose of broad coverage favors retroactivity.

The third factor is a weighing of the equities.[4/] Defendant argues that several hardships weigh against retroactivity: administrative burden, increased claims on the fund, and adverse effects on individual claimants. Administrative burden cannot rise to the level of "substantial inequitable results," Chevron Oil v. Huson, 404 U.S. at 107.

If it did, it could be raised in almost every case where a statute is found unconstitutional. The depletion-of-the-fund argument has not been supported by any evidence. Mere assertions are insufficient. See Hurvich v. Califano, 457 F.Supp. 760, 764 (N.D. Cal. 1978).

The most serious problem in weighing the equities is possible adverse effects on individuals. Defendant argues that reallocation of income may reduce some males' quarters of coverage so as to make them ineligible or reduce their benefits. Defendant also conjectures that some women may be better off with their share of their husbands' accounts than with their own. These difficulties can be avoided, however. This court has the power to fashion a remedy that would "minimize the burdens imposed by a declaration of unconstitutionality upon innocent recipients of government largesse." Califano v. Westcott, 443 U.S. 76, 90 (1979). This court finds it appropriate to order that, despite any recomputation, no current recipient shall have his benefits reduced. Also, the agency is to allow women who would benefit more from the former system to elect to remain under the original allocation.

Application of the Huson test to this case demonstrates that retroactive application of the decision in this case is proper. Therefore, plaintiff class members are entitled to a recomputation of their earnings records, extending back to the beginning of Social Security if necessary. There is no justification for cutting off retroactivity at any prior point.[5]

STATUTORY TIME LIMITATIONS

The Secretary contends that plaintiffs are bound by

§ 405(c)(4) and (5) time limitations on changing entries in employment records. Section 405(c)(4) sets a time limit of three years, three months, and fifteen days within which income entries may be corrected. After that time, the records become conclusive evidence of the amount or existence of self-employment income, § 405(c)(4)(C), unless one of the specific exceptions in § 405(c)(5) is met.

The Secretary cannot use the statutory time limitations to preclude recomputations where the statute has been found unconstitutional. This court has the authority to provide plaintiffs with effective relief.

In addition, plaintiff class members fall into one of the exemptions from the limit, § 405(c)(5)(G).[6] That section allows the Secretary "to correct errors made in the allocation . . . [of] self-employment income." Therefore, the agency is not to restrict class members' requests for reallocation to the three year, three month, and fifteen day period.[7]

AMENDMENT OF REGULATIONS

Plaintiffs have requested that defendant be ordered to adopt regulations that conform with this court's ruling. Plaintiffs also request that any proposed regulatory amendments be subject to review by this court prior to publication. Such an order would be inappropriate. It is expected, of course, that any regulations adopted by the agency will be consistent with the several holdings of this court and other courts that have found § 411(a)(5)(A) unconstitutional. Plaintiffs retain the right to challenge any rule-making by following normal procedures.

## NOTICE TO CLASS MEMBERS

The defendant is ordered to send individual notices of rights under this decision to female class members residing in community property jurisdictions who were denied benefits between August 20, 1980 and April 14, 1981. Defendant estimates that such notice will cost approximately $70,629.00.[8] This court finds that this is not an unreasonable amount, given the importance of the rights involved. Also, defendant was given the opportunity to correct its application of § 411(a) after the decision in Carrasco v. Secretary of Health, Education and Welfare, 628 F.2d 624 (1st Cir. June 11, 1980), and failed to do so. Plaintiffs are to submit a proposed notice that conforms with this and the preceding order of December 17, 1981. Defendant will then have twenty days in which to file objections.

## CONCLUSION

Plaintiff class members are entitled to recomputation of their earnings records through an allocation of co-proprietor income. Each spouse's earnings record should be credited with income proportionate to their labor in the business. The recomputation should extend to any relevant income without time limitations. Notice to class members is to be provided as outlined above.

IT IS SO ORDERED.

January 22, 1982.

MARILYN HALL PATEL

Marilyn Hall Patel
United States District Judge

FOOTNOTES

1/ Hereinafter, all references to section numbers are from 42 U.S.C.

2/ Defendant essentially conceded the unconstitutionality of § 411(a)(5)(A), due to earlier court decisions. Hester v. Harris, 631 F.2d 53 (5th Cir. 1980); Carrasco v. Secretary of Health, Education and Welfare, 628 F.2d 624 (1st Cir. 1980); Becker v. Harris, 493 F.Supp. 991 (E.D. Cal. 1980). Despite those decisions, the agency had continued to apply the challenged section. This court therefore rejected a request by defendant that the case be remanded for consideration, finding that the case-by-case challenge, agency acquiescence, and remand was inappropriate for disposing of these cases. Therefore, plaintiff's motion for class certification was granted.

3/ Defendant has argued that plaintiffs do not have standing to attack the application of the remainder of § 411(a), since it has never been applied to them. This argument has no merit. Standing concerns whether the court has initial jurisdiction to hear a suit. It does not pertain to the later stage of relief.

4/ Even if the equities weighed in favor of prospective application, retroactivity would still be required since the first two prongs of the Huson test have not been met. See Cash v. Califano, 621 F.2d 626, 629 (4th Cir. 1980).

5/ This court is aware that retroactivity in a sex discrimination case has been limited to the date of decision in Frontiero v. Richardson, 411 U.S. 677 (1973), as "the case in which the new principle of law was first enunciated." Cash v. Califano, 469 F.Supp. 129, 135 (W.D. Va. 1979), aff'd, 621 F.2d 626 (4th Cir. 1980). This court finds such limitation inappropriate. The announcement of a new principle of law is relevant to whether retroactivity is appropriate, not to the period of retroactivity.

6/ It has been suggested that § 405(c)(5)(G) applies only when the entire earned amount is being shifted to another account. There is no basis for such a narrow reading of the statute. At least one court has applied that exception to a division of earnings between co-proprietors. See Bocian v. Matthews, 411 F.Supp. 1200 (N.D. Iowa 1976).

7/ It should be emphasized that even if the earnings are reallocated, this is not to adversely affect the benefits of any current recipient.

8/ A slightly higher figure was suggested by defendants at the hearing but that amount did not exceed $90,000.

Chairman PICKLE. Now, we will ask Mr. Eldin Glanz, director of tax relations, to present his testimony.

## STATEMENT OF ELDIN H. GLANZ, DIRECTOR OF TAX RELATIONS, HERCULES INC., ACCOMPANIED BY GARY G. QUINTIERE, COUNSEL

Mr. GLANZ. My name is Eldin H. Glanz, and I am director of tax relations of Hercules Inc., Wilmington, Del.

I am accompanied by Gary Quintiere, counsel for Hercules.

I am here to speak in favor of section 301 of H.R. 7623. That section would make minor modifications to the Social Security Act and Internal Revenue Code for purposes of extending social security and tax-qualifying pension plan coverage to certain U.S. citizens who are employed by foreign employers.

My oral remarks are supplemented by a more detailed written statement which I ask to be made part of the record of these hearings.

Hercules is a multinational corporation conducting business activities in the U.S. and many foreign countries.

Like many such corporations, Hercules must frequently assign domestic U.S. employees to foreign enterprises in which Hercules has an interest in order to properly control those activities or monitor their progress.

Our U.S. employees who are asked to go on foreign assignment are necessarily confronted with a host of problems associated with transplanting one's self and family to a foreign country.

Hercules, through its well-developed expatriate program, is able to deal with and alleviate most of the problems.

However, because of an unexplained and presumably unintended restriction in current law, there are two problems which we cannot satisfactorily resolve, namely, the continuation of coverage of our foreign-based employees in the U.S. Social Security System and Hercules tax-qualified pension and savings plan.

Under current law, if a U.S. corporation assigns one of its employees to a foreign corporation in which it owns 20 percent or more of the voting stock, the U.S. corporation can arrange to continue the coverage of that employee in the U.S. Social Security System. If the U.S. corporation elects to continue the employee's social security coverage, it can also elect to continue the coverage of that employee in the corporation's tax-qualified benefit plans.

Both these benefits can continue to be made available to the employee, even though in actuality he is an employee of the foreign employer and not of the U.S. corporation which assigned him.

The difficulty with the current law, however, is that it is unduly restrictive in three ways. One, current law does not permit coverage where the U.S. employee is assigned by, or assigned to, a business entity which is not a corporation.

Thus, if Hercules were to assign one of its employees to a foreign joint venture organized as a partnership, Hercules could not, under current law, continue social security and tax-qualified benefit plan coverage to that employee.

Two, current law requires that if an employee is assigned to a subsidiary of a foreign corporation, the first tier foreign corporation must own more than 50 percent of the voting stock of its subsidiary. This is a harsh requirement, and unnecessarily restrictive, inasmuch as the required relationship between the U.S. corporation and the foreign parent need only be 20 percent of the voting stock.

Under current law, for example, Hercules can own 100 percent of the voting stock of the foreign parent. But if the foreign parent does not own more than 50 percent of the voting stock, Hercules' employees cannot own stock applied to the sub.

Third, for example, if Hercules owned 100 percent of the voting stock of a foreign corporation *X*, and *X*, in turn, owned 100 percent of the voting stock of subsidiary *Y*, Hercules could not extend social security and tax-qualified benefit coverage to employees working for subsidiaries of *Y*.

The provisions in section 301 of H.R. 7623 would correct the deficiencies in current law and would thereby permit the extension of social security and tax-qualified benefit plan coverage to foreign-based U.S. citizens who presently are excluded from such coverage.

Enactment of these provisions would have only a de minimis effect on the social security system because of the relatively few employees involved.

For the few employees involved, however, the exclusion from the U.S. Social Security System and Hercules tax-qualified benefit plans is a major concern. Accordingly, on behalf of Hercules and its concerned employees, I ask you to report section 301 favorably. It is important that this provision be enacted by the full Congress, and I urge this subcommittee to take the first step.

Thank you for the opportunity to appear before you today. I, or Mr. Quintiere, would be pleased to answer any questions.

[The prepared statement follows:]

## STATEMENT OF ELDIN H. GLANZ, DIRECTOR OF TAX RELATIONS, HERCULES INC.

On behalf of Hercules Incorporated, I want to express my strong support for Section 301 of H.R. 7326—The Social Security Miscellaneous and Technical Improvements Act of 1982. The provisions of Section 301 would extend Social Security and tax-qualified benefit plan coverage to employees of foreign affiliates of American employers. Such extension would be accomplished principally by amending § 3121(1) of the Internal Revenue Code. The reasons for enacting the provisions of Section 301 are set forth below.

### INTRODUCTION

Section 3121(1) of the Internal Revenue Code currently permits a United States corporation (hereafter referred to as a "domestic corporation") to enter into an agreement with the Secretary of the Treasury under which Social Security coverage is extended to United States citizens who are employed by certain foreign subsidiaries of the domestic corporation. A "foreign subsidiary" is defined in § 3121(1)(8) as any foreign corporation of which 20 percent or more of the voting stock is owned by the domestic corporation. A second tier foreign subsidiary may also qualify as a "foreign subsidiary" if "more than" 50 percent of its voting stock is owned by a first-tier subsidiary described in the preceding sentence. Thus, if domestic corporation A owns 20 percent of foreign corporation B, and B, in turn, owns 51 percent of foreign corporation C, A would be able to extend Social Security benefits to United States citizens employed by B or C because both B and C are "foreign subsidiaries" under § 3121(1). If C, however, owned 100 percent of the voting stock of corporation D, domestic corporation A could not extend Social Security benefits to employees of D, because § 3121(1) does not apply to subsidiaries below the second-tier.

### PROBLEM

Under § 3121(1), as now written, Social Security coverage cannot be extended to foreign-based United States citizens if either the domestic or foreign employer is not a corporate entity. The statute uses the word "corporation" which the Department of Treasury has defined to include associations, joint stock companies and insurance companies (Treas. Reg. § 36.3121(1) (1)–1(a) (3)). The Internal Revenue Service has ruled that a "partnership" is not a "corporation" for § 3121(1) purposes (Rev. Rul. 58–14, 1958–1 C.B. 258). Accordingly, Social Security coverage is presently unavailable to numerous United States citizens working for foreign employers, simply because their employer and the domestic affiliate do not conduct their business operations in corporate form. Furthermore, even if the domestic and foreign entities are both corporations, Social Security coverage may still be unavailable if the related corporations cannot meet the "percentage of ownership" requirements or the "tier" requirements.

### BACKGROUND

Section 3121(1) was added to the Internal Revenue Code by § 209 of the Social Security Amendments of 1954 (Public Law 761). One of the primary purposes of those Amendments was to extend Social Security coverage to reasonably large, well-defined groups of persons which were excluded from coverage by then-present law. The Senate Finance Committee report which accompained H.R. 9366 gave the following reason for extending coverage to foreign-based United States citizens who were employed by foreign employers with United States affiliates:

"Under present law, United States citizens working outside of the United States for American employers are covered under old-age and survivors insurance. The bill would extend this coverage to include United States citizens working for foreign subsidiaries of American companies. These provisions would make coverage available to roughly 100,000 United States citizens working abroad for such subsidiaries.

"American employers frequently find it necessary to carry on their operations in other countries through subsidiaries established under the laws of a foreign country. The United States citizens working for such subsidiaries are likely to have the same close economic and personal ties with the United States, and the same expectation of returning to the United States, as do United States citizens working abroad for American employers.

"The coverage of these citizens will prevent the gaps in coverage under old-age and survivors insurance which would otherwise occur when citizens who ordinarily work in covered employment within the United States work abroad for a period for a subsidiary of an American company. Additional disadvantages also arise because workers may refuse to accept employment, realizing that their old-age and survivors insurance protection will suffer if they do so. This new coverage would eliminate these difficulties. (S. Rept. No. 1987, 83d Cong., 2d Sess. 9 (1954). * * *"

It is significant that nowhere in the foregoing report did the Finance Committee indicate that the form of doing business was an important consideration. Rather, the chief consideration expressed in the report was Congress' concern for United States citizens excluded from the Social Security system.

Since the enactment of § 3121(1) in 1954, there have been two important statutory developments. The first occurred in the Social Security Amendments of 1956 (Public Law 880). Section 201(j) of that Act amended § 3121(1) with respect to the minimum voting control which the domestic corporation was required to have over the first-tier foreign corporation in order to qualify for § 3121(1) treatment. The original legislation required the domestic corporation to own more than 50 percent of the voting stock of the first-tier foreign corporation. The 1956 amendment reduced that requirement to 20 percent. The Senate Finance Committee report gives the following reason for the change:

"Under present law United States citizens working outside the United States for foreign subsidiaries of American corporations may be covered under old-age and survivors insurance by means of voluntary agreements between the parent corporation and the United States Government. Coverage is available only to American citizens who are employed either by a foreign subsidiary in which the American corporation holds more than 50 percent of the voting stock, or by another foreign corporation in which such subsidiary holds more than 50 percent of the voting stock. Under an amendment added to the bill by your committee, the present provision would be broadened to make coverage available to American citizens employed by a foreign company in which the American corporation holds 20 percent or more of the voting stock. * * * (S. Rept. No. 2133, 84th Cong., 2d Sess. 13 (1956))."

The second major development concerning § 3121(1) came with the Revenue Act of 1964 (Public Law 88-272). Section 220(a) of that Act added § 406 to the Internal Revenue Code with the result that foreign-based United States citizens covered under § 3121(1) agreements could henceforward be covered under benefit plans which qualified under § 401(a). The rationale for the new Code section was simple: If domestic companies could extend Social Security coverage to United States citizens working for certain foreign-based affiliates, they should be able to cover the same employees under qualified plans. (See S. Rept. No. 830, 88th Cong., 2d Sess. 85 (1964)).

Section 406 solved a substantial dilemma which had troubled American employers for many years. Prior to § 406, it was not possible to include a foreign-based United States citizen in the qualified plan of the domestic parent unless the parent could demonstrate that the employee, through working abroad, continued to be an employee of the parent rather than the foreign company with which he was based. This was necessary because of the "exclusive benefit" rule which requires a qualified plan be maintained exclusively for the benefit of the employer's own employees. If the domestic parent could not describe the foreign-based employee as its employee, then the only way to permit the employee to continue under qualified benefit coverage, which was comparable to that offered by the parent's plan, was for the parent to have the foreign subsidiary adopt the parent's plan. The major drawback in this arrangement, however, was that in order for the foreign subsidiary's plan to qualify under § 401(a), it had to satisfy the coverage requirements of that section. Frequently, those coverage requirements necessitated the plan's inclusion of foreign-born employees. Thus, to continue qualified benefit coverage to the one or two United States citizens temporarily assigned to a foreign affiliate, the domestic parent was often forced to create a separate qualified plan and to include therein, along with the United States citizens, many foreign employees whom the parent had no interest in covering.

Section 406 eliminated these problems by permitting the American employers to treat employees covered by § 3121(1) agreements as their own employees for qualified plan purposes, thus allowing such employees to be covered under the employer's plan without running afoul of the "exclusive benefit" rule.

In summary, a company's ability to enter into a § 3121(1) agreement is important for two reasons: First, it permits the company to cover foreign-based United States citizens under Social Security; and second, if the company has a qualified pension plan, a § 3121(1) agreement is useful in extending qualified plan coverage to those employees.

## SECTION 301 OF H.R. 7326

Section 301 of H.R. 7326 would expand the scope of § 3121(1) by making the following changes:

1. Make the section applicable to all forms of business entities, rather than just corporations;
2. Change the 20/50 percent control requirements to a more flexible requirement which allows for coverage in all cases where the domestic employer has more than a 10 percent direct or indirect interest in the foreign employer; and
3. Allow for coverage below the second-tier subsidiary level.

## REASONS FOR THE CHANGES

Many American companies do not conduct their foreign business in corporate form. Often they work through joint venture partnerships in tandem which one or more domestic or foreign companies. There are also instances where domestic corporations are not able to utilize § 3121(1) and § 406 because their ownership interests in related foreign entities do not meet the rigid voting control tests set forth in § 3121 (1)(8). For example, if domestic corporation A owns 100 percent of the voting stock of foreign corporation B and B, in turn, owns 50 percent of foreign corporation C, A could not enter into a § 3121(1) agreement to cover United States citizens working for C. This is because B does not own "more than" 50 percent of the stock of C. This result is rather anomalous considering the fact that A's indirect interest in C—50 percent—is substantially greater than the minimum indirect control which § 3121(1) presently requires—just over 10 percent. Another problem with § 3121(1) is that it does not extend to employees of affiliated foreign subsidiaries below the second-tier level. This is a limitation which serves no useful purpose.

The changes proposed by Section 301 of H.R. 7326, if adopted, would resolve these problems while keeping the spirit of § 3121(1) intact.

If § 3121(1) is not changed, the American worker will be the party most aggrieved. Interruption of Social Security coverage can be costly to workers and their dependents. In some cases, it can be catastrophic. In addition, foreign employment without the benefit of § 3121(1) may also mean the loss of qualified benefit of plan coverage. Many foreign employers do not offer such plans, while those which do, have plans which are inferior to those offered by the domestic affiliate. Even if the foreign plans were roughly comparable to those maintained by the domestic employer, they would not be equally attractive to temporarily-based United States citizens. Those employees have generally made their financial arrangements in the United States and would be greatly inconvenienced by having their pension benefits administered in a foreign country and paid in foreign currency. The proposed legislation would allow such employees to remain in the qualified benefit plans of their domestic parent.

### CONCLUSION

Section 3121(1) was enacted by Congress in 1954 to close a gap in the then-existing Social Security system. Experience since that time has demonstrated that this legislation did not go far enough and that further legislation is needed. The provisions set forth in Section 301 of H.R. 7326 are consistent with the remedial aims of § 3121(1) and should create no substantive or procedural problems for either the Internal Revenue Service or the Social Security Administration. The one point which needs some further clarification is the operation of § 3121(1) with respect to U.S. employees working in a foreign country which has entered into a totalization agreement with the United States under Section 233 of the Social Security Act, 42 U.S.C. 433 (1970). In our judgment, if a U.S. employer wishes to continue its obligation under a § 3121(1) agreement it should be allowed to do so, irrespective of a concurrent totalization agreement. (See, however, Rev. Rul. 79-232, 1979-2 C.B. 359). At minimum however, if a totalization agreement is viewed as overriding a § 3121(1) agreement, the U.S. employer should still be able to continue benefit plan coverage to affected employees under § 406.

Chairman PICKLE. Thank you, Mr. Glanz. I know you are in favor of extending coverage in this area. But you do make three suggested changes which you say would not affect the strength of the system, itself, or would not hurt it, anyway.

We will take those under consideration. I have not had a chance to look into them and will not take the time to this afternoon, but we appreciate your testimony and your suggestions.

Now we will hear from Mr. Paul Jackson, consultant and vice president and actuary of the Wyatt Co., representing the National Small Business Association.

Mr. Jackson.

## STATEMENT OF PAUL H. JACKSON, CONSULTANT, VICE PRESIDENT AND ACTUARY, THE WYATT CO., ON BEHALF OF THE NATIONAL SMALL BUSINESS ASSOCIATION

Mr. JACKSON. Thank you, Mr. Chairman. I am representing today, the National Small Business Association, which is a multi-industry trade association representing 50,000 small- and medium-size firms throughout the country. I am also appearing on behalf of NSB's affiliated Small Business Legislative Council which represents approximately 4 million small business owners through its 69-member trade and professional associations.

We always appreciate the opportunity to present our views on social security. It is a program that small business supports and relies upon. First with regard to title I of H.R. 7326, we strongly support intelligent cash management and the changes proposed in the legislation. Indeed we would prefer to see greater flexibility in the selection of the appropriate investments for the program.

Specifically, in section 103 of H.R. 7326 the trust funds are to be invested in government bonds having maturities of more than 4 years, or less than 4 years depending on which class has the greatest average market yield. We believe the law should be more flexible in this regard and permit investment in either class where that might be necessary due to the cash flow requirements of the programs or because of investment considerations. For example, from the standpoint of investment theory, long-term bonds should, on most occasions, bear a market yield in excess of that of short-term bonds because of the added risk of price fluctuation. If the additional yield were inadequate to compensate for this added risk, section 103 would still appear to require investment in longer term bonds. Accordingly, we believe that the trustees should be permitted some discretion in their choice of security.

As to title II of H.R. 7326, we support in principle all of the changes that would eliminate unfair distinctions that are based solely upon sex. We believe the costs of these specific changes would be minimal. If they were not, however, we believe they should be considered in concert with the general financial reform of social security.

### TAX TREATMENT OF 401(k) PLANS

We are quite concerned with the administrative problems which we see created by section 304 of H.R. 7326. We believe that the problems caused by the proposed taxation of contributions to cash or deferred profit-sharing plans under section 401(k) of the code would significantly outweigh the financial advantage of taxing these contributions.

As you may recall, subject to certain stringent restrictions, section 401(k) of the code provides that a qualified profit-sharing plan may permit a participant to make either of the following two choices:

### CASH IN LIEU OF DEFERRAL

The participant may choose to receive in cash a portion of the employer contribution that would otherwise be contributed to a profit-sharing plan and thus deferred. Such a choice subjects amounts so received to Federal and FICA tax.

### DEFERRAL IN LIEU OF CASH

Alternately, the participant may choose to defer a portion of compensation that would otherwise be received in cash. This is effected by a salary reduction agreement with the employer under which the deferred amount is paid by the employer to a qualified profit-sharing plan. This avoids payment of current income and FICA tax on the amount deferred.

Contributions to such plans traditionally have come from funds which employers have made available as part of their retirement and deferred compensation programs. These amounts, similar to other defined contribution pension plans, are generally determined annually by the employer in consideration of the needs of his employees, his own financial situation, and the competitive practices of other employers. More recently, a number of companies have adopted plans which allow employees to reduce their own direct compensation and contribute such salary reduction amounts to a 401(k) plan. Since the proposed legislation addresses only taxation of contributions to 401(k) profit-sharing plans, and not other traditional profit-sharing or pension plans, it must be assumed that the real concern of Congress is with revenue erosion for the social security system due to salary reduction arrangements—rather than the fact that all contributions to retirement plans are not taxed.

While it is true that such salary reduction arrangements will result in some lessening in FICA tax receipts—as well, it should be noted, as a future reduction in social security payments—we feel that there are two very significant reasons why such salary reduction arrangements should not be subject to FICA taxation.

First, in the attempt to subject salary reduction contributions to 401(k) plans to FICA taxes, all company contributions have been subjected to the tax. This is inconsistent with the treatment of all other contributions to qualified profit-sharing and pension plans.

Second, that the demands on our payroll, accounting and other administrative functions will be significantly increased by the practical requirements of the implementation of this law.

I would like to address each of these issues in turn.

Enactment of the proposed legislation would subject all profit-sharing contributions being made by companies to profit-sharing plans qualified under section 401(k) to social security tax for the first time. Clearly it is not the intent of Congress to subject to social security taxes contributions to all qualified profit-sharing and pension plans. The singling out for taxation of one type of plan seems to make no sense. It should be noted that cash and deferred profit-sharing plans are of particular interest to small business because of their ease of administration and responsiveness to the needs of the workforce. While a large employer may be able to put into place different plans to address the varying needs of his employees, small business often can only offer one plan. The flexibility inherent in a 401(k) plan make such plans particularly appropriate for such small business needs.

You might respond that you do not intend to tax profit-sharing contributions, your concern is to stem the tide of revenue loss due to salary reductions, and therefore you will revise this proposed legislation in such a way that it only taxes salary reductions.

Unfortunately, it has clearly been demonstrated that it is not possible to distinguish salary reduction contributions to a profit-sharing plan from traditional profit-sharing contributions. The fact is, compensation is fungible. It is impossible to draw practical distinctions among the forms of compensation that can serve as sources of contributions for 401(k) plans prior to their actual distribution in a specific form—that is, cash or deferral. Any artificial rule that is drawn to subject one particular source of funds—salary reduction—to FICA taxation will cause employers to rearrange their compensation programs to avoid such taxation and thereby defeat the attempted additional taxation.

As an example, let's look at two companies. One company is currently offering a salary for a particular position of $20,000 a year and no retirement benefits. The other offers a salary for the same position of $19,000 a year and also provides an annual contribution of $1,000 to a profit-sharing plan. Each employer feels that it would be appropriate to provide his employee with more control over the extent to which compensation is received in the present or deferred. Therefore, each implements a 401(k) profit-sharing plan. It would seem impossible to have equity when the employee of the first company, if he chose to deposit $1,000 to the plan, was forced to pay social security tax on his contribution since it was coming from a salary reduction, while the employee of the second firm, if he chose the $1,000 deferral, would not be subject to that taxation. Alternately, it would seem unfair to tax contributions from both of these firms when a third firm, which had not taken the initiative of making its programs more responsive to the needs of its employees and therefore did not implement a 401(k) plan, was not subject to taxation.

The second major area of concern that we have is the required recordkeeping and administration for the implementation of this proposed legislation. It would be necessary to make significant changes in two major areas. These are:

First, the payroll system or payroll process, and second, the recordkeeping associated with contributions to qualified profit-sharing trusts.

All payroll systems would have to be modified to be able to calculate and maintain a second and different taxable income figure. Our payroll systems are already staggering under the load of having to calculate, maintain and report Federal income taxes, social security taxes, FUTA taxes, State taxes, and city taxes. At least now all of these taxes are applied against the same gross earnings. The necessity of having different earnings figures for social security and Federal tax purposes greatly complicated the administrative complexity of payroll accounting. It must be realized that each of these earnings figures propagates itself through the system and appears in numerous forms and calculations. The possibility for confusion, misinterpretation and inaccurate payroll administration is significantly compounded by having different annual earnings figures. One can imagine the nightmare which would occur as Federal, FICA, FUTA, State, and city tax codes each seek to establish their own criteria of inclusion and exclusion from taxation. The cost of the necessary modifications to procedures, computer systems, paycheck stubs, reporting forms, and the cost of explanation and communication to all of our employees would probably dwarf the revenue enhancement which would be possible by the implementation of this change.

The administrative problems associated with social security taxation of profit-sharing contributions not processed through the payroll system are even more difficult. Currently, when contributions are made to a profit-sharing plan one check is made out to the trustee. Mechanisms for the separate calculation and allocation of FICA tax would have to be developed. This system would have to be carefully coordinated with the payroll system to insure that taxation in excess of the wage base did not occur. Employees would be subjected to withholding on amounts which they had never received in cash.

With the implementation of section 401(k) of the code, the Congress has provided small business with a tool which enables it to offer deferred compensation and retirement programs which can be responsive to the needs of their employees without the necessary complications and administrative burdens associated with the implementation of a number of different plans as oftentimes offered by major employees.

The enactment of this legislation will make the administration of 401(k) plan such an onerous burden that a valuable tool will be lost to small business.

Thank you for your consideration.

Chairman PICKLE. Mr. Jackson, I thank you. I guess we agree generally on most of the bill, except you don't want to pay that FICA tax. Do we have that many—you said it would impose a heavy burden on the employers since it would be forced to distinguish between which employees participate in the plan and which do not.

Do you have that many of those plans in the country that this would be an administrative problem?

Mr. JACKSON. I think there are a good many of these plans.

Chairman PICKLE. Do you know how many?

Mr. JACKSON. What we are talking about, you see, is the profit-sharing plans that existed before the code was expanded that permits salary reduction. My own company, the Wyatt Co., has a profit-sharing plan. After employees have been participants in the plan for 2 years, they have an option of taking a part of the following year's contribution in cash rather than having it added to the program.

Now that money was never in their pay, and nobody reduced their pay to get the amount into the fund that is going in. They are taking, in effect, money out of the fund and paying a current tax on it. It is that kind of a plan that I think is fairly prevalent.

As I say, if social security taxes were to be levied on the employer dollars that go into that plan for all of the people who do not take the cash, when maybe only 5 percent want the cash, the only solution to the problem from our standpoint would be to eliminate the cash option entirely. And then no part of the contribution would be subject to FICA taxes by this rule; in other words, a profit-sharing plan without an option to receive a portion of the money in cash would not be subject to FICA taxes.

Chairman PICKLE. Well, the purpose of our bill is to try to deal with plans that give an option to the employee to either take his cash or have deferral. We are saying that since he has an option, that it is our opinion that that amount should be subject to social security taxes. You would disagree with that?

One, you say it would be administratively difficult to handle. We don't think there are many cases like that in the country. It might be complicated if he has a choice bringing it out part cash and part deferral. I can see that. But it seemed to me that once he makes that choice, then he would be subject to the tax. If we were to enact this section 304, we would hope that it would actually simplify the bookkeeping for the various employers because of the treatment on FICA taxes would be the same regardless of whether it was received in cash or put into the plan.

I do want to know what kind of problem it would create, if indeed it affects a lot of companies. We would be willing to receive testimony from other companies or additional testimony from you as we go along.

Mr. **Jackson**. I would just like to point out, sir, that when you say it would simplify it because it would subject to FICA taxes a given sum of money, whether that sum of money were deferred or received in cash, it would have the effect of subjecting certain amounts of money to FICA taxes and income taxes, and other amounts of money to FICA taxes alone and not withholding taxes.

So withholding would have to be different between the two pieces. That is the problem with the 401(k) situation, the salary reduction plan. In other words, it creates an administrative problem. A good many of these small companies, for example, have payroll systems that are manual. They just write things out. This is a complexity, and somebody has to be taught to do it right.

A good many other ones use their local bank to develop a payroll system and so on. This would double the work, because the employer would have to keep track of two gross income amounts, one that is subject to FICA taxes, and a smaller one subject to Federal income tax withholding.

Chairman **Pickle**. Well, you are active in this field, and we would be glad to receive other statements from you. We had hoped that this approach might simplify matters. If you have any additional statement, we would be glad to receive it.

I don't believe this provision is controversial or complex. But if you feel that way we would be glad to hear from you and others.

[The following was subsequently received:]

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December 16, 1982

COMMITTEE ON
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WAYS AND MEANS

Mr. John J. Salmon
Chief Counsel
Committee on Ways and Means
U.S. House of Representatives
Longworth Office Building
Washington, D.C. 20515

Re: December 6, 1982 Hearings on H.R. 7326

Dear Mr. Salmon:

Enclosed is the transcript of my testimony on December 6, 1982 with the necessary corrections inserted therein. In my testimony, I suggested that while the Committee may have in mind taxing, as Social Security wages, those amounts of salary reduction which employees have elected to have put into a deferred profit sharing plan or defined contribution pension plan for them, the plans described in 401(k)2 include a good many other types of arrangements. A number of qualified profit sharing plans have offered participants the right to receive in cash a portion of the employer contribution that would otherwise be deferred. H.R. 7326 would subject to FICA taxation all employer contributions to such plans, not just those subject to a 401(k)2 election.

We have attempted to estimate the number of such plans that might now be in existence. We were unable to find any extensive surveys incorporating this information. A 1982 sample survey conducted by the Profit Sharing Council of America showed that, of the 521 plans which responded, 425 offered deferred benefits only, 13 offered only cash benefits, and 83 a combination of cash and deferred benefits. Thus, about 16% of those plans contain an arrangement described under Section 401(k)2 of the Internal Revenue Code and therefore would have all contributions subjected to Social Security taxation. At the end of 1982 there were approximately 337,000 profit sharing plans in the United States, and if this same percentage were to apply, perhaps 50,000 of such plans would contain arrangements described in Section 401(k)2 of the Internal Revenue Code and have all contributions subject to the taxation required by Section 304 of H.R. 7326.

We have gone through some of the files in our Information Retrieval Center covering these employer programs (Industry Retirement Practices Series of ERISA Benefit Funds, 515 National Press Building, Washington, D.C.). A brief description of some of these plans offering cash options is attached hereto in case your Committee wishes to check any of this information.

If an employer has such a cash or deferred profit sharing plan, it is likely that it started out as a pure deferred profit sharing plan. Then, at a later date, pressure from rank-and-file employees for some portion to be paid in cash has resulted in the addition of a cash option for part of the total. In the case of our own deferred profit sharing program, employees who have participated for two years in the plan have the right to elect to get up to one-third of the employer contribution to the plan diverted from the fund itself and paid to them in cash. Approximately 15% of the employees covered under our plan take advantage of this cash option. If all of the employees covered under the plan were subjected to Social Security tax on 100% of the employer contribution, or even on one-third of it by reason of the desire of 15% of the group to receive cash, we would undoubtedly eliminate the cash option and revert to a pure deferred program. This would eliminate a valuable benefit for some of our employees who find themselves in current financial need. It would also reduce, rather than enhance, the revenue received by the Social Security system since the money which the employees are now taking in cash would instead be added to the fund, thereby eliminating even the present cash payments from Social Security taxation. Other employers, where greater numbers are taking advantage of the cash option, might simply pay the cash to everyone and make the deferred portion a pure deferred program with no cash option at all.

We do not believe that an effort at this time to stem the loss of Social Security revenue by reason of salary reduction arrangements should, through inadvertence, incorporate in the Social Security taxation all sorts of programs that have never been set up on a salary reduction basis. Neither do we believe that your proposed legislation should be the cause for the elimination of cash options under cash and deferred plans.

If the Committee wishes to explore this matter further, we would certainly be glad to answer any questions you might have. Alternatively, you might wish to get in touch directly with the Profit Sharing Council of America, 20 North Wacker Drive, Chicago, Illinois 60606. The President is Mr. Walter Holan. Another possibility is the Profit Sharing Research Foundation, 1718 Sherman Avenue, Evanston, Illinois 60201, where Mr. Burt L. Metzger is President and Secretary. Both of these gentlemen are well versed in the prevalence of various provisions in profit sharing plans, as well as the likely response of profit sharing sponsors to potential changes in the legislative or tax environment surrounding those plans.

Again, let me express on behalf of the National Small Business Association and the Small Business Legislative Council, our appreciation for the opportunity to set forth our views on the provisions under H.R. 7326.

Sincerely,

Paul H Jackson

Paul H. Jackson
Consulting Actuary

PHJ:cd
Enclosures

cc: Mr. Herb Liebenson
Mr. Walter Holan
Mr. Burt Metzger

INDUSTRY: CHEMICAL

COMPANY: Stepan Chemical Company
Northfield, IL

SIC: 2873

DATA VERIFIED BY PLAN SPONSOR: March, 1981
(Month, Year)

(PROFIT SHARING)

| | |
|---|---|
| PLAN NAME: | Profit Sharing Plan |
| APPROXIMATE NUMBER OF PLAN PARTICIPANTS: | Active: 266<br>Retired/Separated: N/A |
| ELIGIBILITY FOR PARTICIPATION: | Salaried employees become participants on the first day of the month following completion of 3 consecutive years of service. |
| EMPLOYEE CONTRIBUTIONS: | Non-contributory. |
| EMPLOYER CONTRIBUTIONS: | The basic company contribution is lesser of 5% of net profits, or 5% of earnings* of all participants. In addition, the board of directors of the company may, as it deems appropriate, make a supplemental contribution to the profit sharing plan in each year. The amount of the contribution is dependent upon the profits of the company during each plan year subject to limits set by federal law.<br>*Earnings are basic cash compensation excluding bonuses, overtime and all other forms of additional compensation. |
| DISTRIBUTION OF EMPLOYER CONTRIBUTIONS: | Each year the employer contribution is allocated to each participant as his earnings relate to total participant earnings.<br>At least 30 days prior to the end of any plan year, a participant may file a written request with the committee electing to receive a cash payment from the company of an amount equal to 33-1/3% of the amount allocated to his account. |
| VESTING: | Full immediate, 100%. |
| INVESTMENTS: | Trust held by the First National Bank of Chicago. |
| WITHDRAWALS: | Except for the annual cash payment election, participants cannot receive payment from their accounts until employment termination. |

INDUSTRY: CHEMICAL
COMPANY: Stepan Chemical Company
PLAN: Profit Sharing Plan
PAGE 2

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| | |
|---|---|
| FORM OF PAYMENT: | A lump sum or a series of substantially equal annual or more frequent installments over a period not to exceed 15 years. The form of payment is decided by the committee after consultation with the participant and shall not begin later than 60 days following the date of the close of the plan year during which the participant reached 65, or terminated employment. |
| EFFECTIVE DATE OF PLAN: | 1/1/76 |
| DATE OF LAST AMENDMENT: | 1/1/80 |

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INDUSTRY: COMMERCIAL BANKING

COMPANY: Chase Manhattan Bank, N.A.
New York, NY

SIC: 2090

DATA VERIFIED BY PLAN SPONSOR: December, 1980
(Month, Year)

(PROFIT SHARING)

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| | |
|---|---|
| PLAN NAME: | Thrift-Incentive Plan (T.I.P.) |
| APPROXIMATE NUMBER OF PLAN PARTICIPANTS: | Active: 16,000<br>Retired/Separated: 574 |
| ELIGIBILITY FOR PARTICIPATION: | 12 months of service and received credit for 1,000 hours of service during the 12-month period after date of employment. Staff members who are employed on an unscheduled basis are not eligible to participate. A staff member who meets the eligibility requirements becomes a participant in the plan on the first day of the next valuation period. There are three valuation periods each year - one beginning January 1, one beginning May 1, and one beginning September 1. |
| EMPLOYEE CONTRIBUTIONS: | Optional, 2%, 4%, 6%, 8%, or 10% of annual regular basic compensation. |
| EMPLOYER CONTRIBUTIONS: | Under the previous Thrift-Incentive Plan formula, Chase's contribution to TIP equaled 6% of the corporation's net applicable income. This was net income before income taxes and before securities gains and losses, but after certain adjustments. These adjustments included the restatement of tax-exempt income as if the income was fully taxed as well as the exclusion of income (or losses) of non-participating subsidiaries. The TIP allocation percentage was derived from the contribution amount divided by participants' eligible salaries.<br>The new formula has two factors: Return on Common Equity (ROCE) and earnings growth. ROCE is income before securities gains (or losses) less preferred dividends divided by average common stockholders' equity. ROCE provides for a minimum (or base) TIP allocation as shown below. Earnings growth is the percentage by which income before securities gains has grown from the previous year. Any year in which the base determined by ROCE is below the 15% TIP allocation maximum, earnings growth may provide an additional allocation. These two combined factors determine the TIP allocation percentage for each participant. |

INDUSTRY: COMMERCIAL BANKING
COMPANY: Chase Manhattan Bank, N.A.
PLAN: Thrift-Incentive Plan (T.I.P.)
'AGE 2

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The TIP allocation derived from ROCE is shown in the table below. When the actual ROCE figure falls between whole percentages, the TIP contribution will reflect that. For example, if ROCE is 12.5%, the TIP contribution based on ROCE will be 12.5%. This proportional adjustment is known as interpolation.

| If Return on Common Equity is: | TIP Contribution Derived from ROCE will be: |
|---|---|
| 15% or more | 15% of participant's eligible salary |
| 14% | 14% of participant's eligible salary |
| 13% | 13% of participant's eligible salary |
| 12% | 12% of participant's eligible salary |
| 11% | 11% of participant's eligible salary |
| 10% | 10% of participant's eligible salary |
| 9% | 7.5% of participant's eligible salary |
| 8% | 5% of participant's eligible salary |
| 7% | 2.5% of participant's eligible salary |
| 6% | - |

The TIP allocation will also include the following additions when annual earnings have increased over the preceding year. This figure is also subject to interpolation, meaning that if earnings growth is 12.5%, the portion of TIP derived from the table below would equal 2%.

| If Annual Earnings Growth is: | Additional TIP Contribution Derived from Annual Earnings Growth will be: |
|---|---|
| 25% | 4.0% of participant's eligible salary |
| 20% | 3.2% of participant's eligible salary |
| 15% | 2.4% of participant's eligible salary |
| 10% | 1.6% of participant's eligible salary |
| 5% | .8% of participant's eligible salary |
| 1% | .16% of participant's eligible salary |

To illustrate: If ROCE were to equal 12.25% in any year, the TIP contribution derived from ROCE would also equal 12.25%. In that same year, if earnings growth was 13.7% over the previous year, an additional contribution would be made to TIP of 2.19%. These two percentages - 12.25 plus 2.19 - would then be added together to determine the total Chase allocation for that hypothetical year of 14.44% of eligible salary.

The 1980 and 1981 allocations will be calculated under both formulas and whichever results in the larger allocation will be used. Not until 1982 will the new formula stand alone.

DISTRIBUTION OF EMPLOYER CONTRIBUTIONS:

Employers' contributions are allocated to participants in proportion to their regular basic compensation while they are participants (see above). 10%, 20%, 30%, 40%, or 50% of the employer's contributions may be taken in cash as elected by

INDUSTRY: COMMERCIAL BANKING
COMPANY: Chase Manhattan Bank, N.A.
PLAN: Thrift-Incentive Plan (T.I.P.)
PAGE 3

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the employee once a year. The balance is put in the employee's deferred allocation account for investment.

VESTING: 100% immediately.

INVESTMENTS: By employee choice -

(1) Bond Fund - governmental or corporate obligations, certain collective trust funds maintained by the Bank for the collective investment of funds of pension, profit sharing or other employee benefit plans, trust and participation certificates which are obligations of an obligor, mortgages and similar interests in improved realty, notes and other evidences of indebtedness, secured or unsecured (excluding specifically obligations of employers), wherever situate even though the same may not be legal investments for trustees.

(2) Diversified Fund - investment in any property, real or personal, or part interest therein, including, but without being limited to, shares of preferred and common stocks; interests in gas or oil properties and royalty and similar interests in property; governmental, corporate or personal obligations; certain collective trust funds maintained by the Bank for the collective investment of funds of pension, profit sharing or other employee benefit plans, trust and participation certificates of deposit, leaseholds, fee titles, mortgages and other interests in improved and unimproved realty; notes and other evidences of indebtedness or ownership secured or unsecured (excluding specifically shares and obligations of employers), wherever situate, even though the same may not be legal investments for trustees. It is intended that not more than 66-2/3% thereof be invested in common stock.

(3) Stock Fund - the same securities or other property as are authorized for the Diversified Fund. It is intended that the investment policy of the Stock Fund emphasize capital appreciation rather than income.

(4) Short-Term Fixed Income Fund - funds invested in obligations issued or fully guaranteed as to the payment of principal and interest by the United States of America having a maturity date not later than 12 months after the date of purchase, or in time or demand deposits with banks (including the Bank), or commercial paper or part interests therein, or certain collective trust funds maintained by the Bank for the collective investment of funds of pension, profit sharing or other employee benefit plans.

(5) The Corporation's Stock Fund.

INDUSTRY: COMMERCIAL BANKING
COMPANY: Chase Manhattan Bank, N.A.
PLAN: Thrift-Incentive Plan (T.I.P.)
PAGE 4

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Permissible Changes: Participants in the plan may elect once in each valuation period (four months) to transfer all or any portion of the existing balances in their deposit and/or deferred allocation accounts to other investments funds.

Voting Pass Through: Yes.

**WITHDRAWALS/LOANS:**

Employee with 5 years of credited service can withdraw any amount in excess of the last two Chase contributions to the deferred allocation account. Withdrawals in excess of the participant's contributions are subject to penalty. This penalty is applied as a reduction of the portion of the next allocation(s) of the employer's contributions to be contributed to the trust for the account of such participant. The reduction is equal to 5% of the amount withdrawn if employee has 10 or more years of credited service or 6% of the amount withdrawn if the employee has less than 10 years of credited service.

**FORM OF PAYMENTS:**

A total distribution is made to employee at termination or retirement, and to his beneficiary at employee's death, in the following forms:

(1) a lump sum, and/or
(2) regular or irregular installments over a period of time, but not past age 80. If any or any part of the account balances are invested in the corporation's stock fund, the employee may elect to receive that part in shares of common stock of the Chase Manhattan Corporation.

**EFFECTIVE DATE OF PLAN:**

12/31/52

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INDUSTRY: COMMERCIAL BANKING

COMPANY: Citicorp
New York, NY

SIC: 6090

DATA VERIFIED BY PLAN SPONSOR: November, 1980
(Month, Year)

(PROFIT SHARING)

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| | |
|---|---|
| PLAN NAME: | The Staff Incentive Plan |
| APPROXIMATE NUMBER OF PLAN PARTICIPANTS: | 15,900 participants of which 5,700 have deferred their benefits and 10,200 are receiving cash. |
| ELIGIBILITY FOR PARTICIPATION: | All eligible staff members after completing two years of credited service. |
| EMPLOYEE CONTRIBUTIONS: | Voluntary contributions of ($2.00 to $10.00 depending on payroll period) up to 10% of salary are allowed only if the employee has invested the entire profit sharing amount for any plan year. A lump sum deposit is also allowed once a year for any period after 6/1/72 for which the employee was eligible to make voluntary contributions but didn't. |
| EMPLOYER CONTRIBUTIONS: | An amount equal to the annual percentage growth in corporate earnings per share; maximum payable is 15% of covered salary. |
| DISTRIBUTION OF EMPLOYER CONTRIBUTIONS: | The employer contribution is all allocated among employees on the basis of their base salary. When employee first joins the plan, he must take his share in cash. On the first day of the year after the employee's third anniversary, the employee may elect to invest all or part of the contribution (in 25% multiples) with the balance received in cash. |
| VESTING: | 100%, immediately. |
| INVESTMENTS: | By employee choice in multiples of 25%:<br>Fund A - fixed income securities including corporation, government and other bonds.<br>Fund B - Citicorp market value common stock. Voting rights are not passed through to the employee.<br>Fund C - In diversified equity investments. |

INDUSTRY: COMMERCIAL BANKING
COMPANY: Citicorp
PLAN: The Staff Incentive Plan
PAGE 2

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Fund D - Citicorp book value common stock.

Changes in investments or shifts of past allocations are allowed once in any 6-month period.

WITHDRAWALS/LOANS:

Withdrawals from Voluntary Contributions

Allowed once in any calendar year. If withdrawal includes any earnings on the voluntary contributions, then the earnings are subject to a 5% penalty. The 5% will be deducted from future profit sharing.

Withdrawals from Contributions by Employer

Hardship Withdrawals - with the consent of the committee, all or part of the profit sharing investment account can be withdrawn without penalty for the following reasons:

1. serious illness or injury to a member of family,
2. housing cost for family,
3. education for family.

Loan Provision

Effective 3/31/80, all participants may borrow against their deferred investment accounts in amounts no less than $500. Loans are limited to 100% of value of participant's deferred account less employer contributions during immediately preceding 2-year period. Loan repayments are made through payroll deductions and include a 5% interest charge (tax deductible). No more than one loan may be outstanding at a time. Full lump sum repayment of unpaid balance of the principal may be made any time.

FORM OF PAYMENT:

After employee's service is terminated with Citibank, he or his beneficiary can receive the full value of his account in one of two ways:

In a lump sum right away or at any time within 5 years after service ends. While this one-time payment can be in cash, employee may take shares of Citicorp stock instead of cash for investment in Fund B. Any investment in Fund A or in Fund C must be taken in cash.

OR

Employee can take his money in equal installments over any period he wants, up to 15 years. During this period profit sharing remains invested in the fund or funds of his choice. Payments can start whenever employee decides, but not later than 5 years after service ends. As in the case of a lump sum payment, he can take equal installments of Citicorp stock for any investment in Fund B.

INDUSTRY: COMMERCIAL BANKING
COMPANY: Citicorp
PLAN: The Staff Incentive Plan
PAGE 3

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|  |  |
|---|---|
|  | The committee has the right to make the final decision on on the way employee collects his money.<br>If employee doesn't give any preference to the committee when he leaves, his share will be paid out in cash. This payment will be made no later than 60 days beyond the year employee reaches 65. |
| EFFECTIVE DATE OF PLAN: | 1/1/52 |

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INDUSTRY: COMMERCIAL BANKING

COMPANY: Crocker National Bank
San Francisco, CA

SIC: 6090

DATA VERIFIED BY PLAN SPONSOR: December, 1980
(Month, Year)

(PROFIT SHARING)

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PLAN NAME: Profit Sharing and Investment Plan

APPROXIMATE NUMBER OF PLAN PARTICIPANTS:
Active: 8,200
Retired/Separated: 15 (installment option)

ELIGIBILITY FOR PARTICIPATION: If employee completes at least 3 years of employment (20 or more hours per week), he is eligible to participate in the plan, provided he is employed as of November 30.

EMPLOYEE CONTRIBUTIONS: Voluntary following the year in which the employee becomes a participant, up to 10% of annual pay. Maximum voluntary contribution may not exceed 10% of employee annual pay for all years of the employee's participation. Each voluntary contribution is submitted by check.

EMPLOYER CONTRIBUTIONS: Determined by the board of directors in its discretion and are a portion of the income of the bank and its consolidated and non-consolidated participating subsidiaries. For purposes of the plan, income means the income before income taxes and security gains of Crocker National Bank and its consolidated subsidiaries, plus the income before income taxes of each non-consolidated participating subsidiary.

DISTRIBUTION OF EMPLOYER CONTRIBUTIONS: One-half of the employer's contribution may be taken in cash each year, and one-half deposited in the profit sharing account. 25% of the employee's portion may be deferred and deposited in the employee's deferred cash account (separate from the profit sharing account). The employee must receive 25% of the total contribution in cash.

An employee's share of the employer's contributions to the plan is based on annual salary. The employee is assigned one unit of value for each full $100 of annual pay, excluding bonuses, but including overtime and shift differentials. Annual pay is defined as pay from January 1 through October 30, plus 20% of that total. Each employee's amount of profit for the year is determined by this formula:

$$\text{Bank's Contributions} \times \frac{\text{individual employee's units of value}}{\text{total units of value of all plan participants}}$$

INDUSTRY: COMMERCIAL BANKING
COMPANY: Crocker National Bank
PLAN: Profit Sharing and Investment Plan
PAGE 2

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| | |
|---|---|
| VESTING: | 100% immediately. |
| INVESTMENTS: | A trust fund with investments in stocks, bonds and other vehicles. Up to 50% of the value of the trust fund may be invested in bonds and the capital stock of Crocker National Corporation, although no voluntary contributions of employees may be used.<br>Voting Pass Through: No. |
| WITHDRAWALS: | Not permitted*, except that part or all of voluntary contributions may be withdrawn, with the consent of the employee benefits committee.<br>*There is one exception: if employee participates in the bank's Long Term Disability Program, at his request he will receive full payment form the plan. |
| FORM OF PAYMENT: | According to employee choice at retirement or termination, or to choice of beneficiary at employee's death:<br>1. Lump sum payment (at time of retirement or deferred for one year), or<br>2. Installments over a period of years. |
| EFFECTIVE DATE OF PLAN: | 1/1/64 |

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INDUSTRY: COMMERCIAL BANKING

COMPANY: Continental Illinois Corporation
Chicago, IL

SIC: 6060

DATA VERIFIED BY PLAN SPONSOR: December, 1980
(Month, Year)

(PROFIT SHARING)

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| | |
|---|---|
| PLAN NAME: | Cash Profit Sharing (This plan replaced the Profit Sharing Trust, also called the Deferred Profit Sharing Plan, as of January 1976. Although no contributions are made to the Deferred Profit Sharing Plan, established January 1, 1960, it still remains in effect for its members.) |
| APPROXIMATE NUMBER OF PLAN PARTICIPANTS: | Active: 8,500<br>Retired/Separated: N/A |
| ELIGIBILITY FOR PARTICIPATION: | A U.S. paid salaried employee automatically participates as of the first December 31 after he has completed at least 10 months of continuous service, provided he is employed on that date. If an employee starts work in January or February or on the first business day of March, he participates in that year's profits. But if he starts after the first business day in March, he will not participate until the end of December of the following year. |
| EMPLOYEE CONTRIBUTIONS: | Non-contributory. |
| EMPLOYER CONTRIBUTIONS: | The company sets aside 6% of its net earnings (including contributions to plan and excluding extraordinary expenses and income tax) for the plan each year, provided that this contribution does not reduce its net operating earnings below 6% of capital.<br>The other participating affiliates of CICorp set aside an amount large enough to assure their eligible employees of the same rate of profit sharing as bank employees receive. |
| DISTRIBUTION OF EMPLOYER CONTRIBUTIONS: | Through 1979 each share was paid in cash after the first of the year, with federal income taxes, social security taxes, and, where applicable, state and local income taxes, withheld. Beginning with the 1980 share, payable February, 1981, the participant may choose to place in a tax-sheltered investment account, held in trust for deferred payment, up to 5% of his base salary (in multiples of 1).<br>Each employee's share is figured in three steps: |

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The first step. An employee shares in the profits in proportion to the base salary he received during the year, not including such extra income as overtime and shift differential pay, suggestion awards, and tuition refunds. The maximum for this first step is 3% of base salary.

The second step. An employee shares in the profits in proportion to that part of base salary in excess of the "adjusted wage base." The adjusted wage base is determined by multiplying the prior year's wage base by the following fraction:

$$\frac{\text{prior year's average salary of all plan participants}}{\text{2 years' prior average salary of all plan participants}}$$

Only the part of salary, if any, that is over the adjusted wage base is considered in this step. The maximum for the second step is 7% of any such part.

The third step. An employee shares in what is left in proportion once again to the base salary received during the year.

The total share is the sum of the results of these three steps.

| | |
|---|---|
| VESTING: | 100% immediately. |
| DEATH: | If an employee dies during the year, the beneficiary receives his allocated share. |
| EFFECTIVE DATE OF PLAN: | 1/1/76 (See comment above with "Plan Name".) |

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summary
plan
description

# Profit Sharing Plan for U.S. Employees

THE *Wyatt* COMPANY

## INTRODUCTION

As an employee of The Wyatt Company your efforts contribute to the profitability of the Company. This Plan makes it possible for you to share in the profits of the Company each year. It provides additional income for you at retirement or in the event of severe financial need. It also provides a sound means of investing some of your own money if you elect to make voluntary contributions to the Plan.

The provisions of the Plan are described on the following pages in informal language for the convenience of you, your relatives and beneficiaries. You should read it carefully, and keep it with your other summary plan descriptions for future reference. If you have any questions about the Plan which are not answered in the booklet, your office manager will be glad to discuss them with you.

## Eligibility

You become a participant in this Plan when you begin working as a salaried employee, if you live and work in the United States. Employees who are residents of Canada are not eligible to participate in this Plan.

## Special Terms - What They Mean

Throughout this booklet you will come across words or terms which affect your benefits. Knowing what they mean will help you to understand your benefits better.

### Compensation

For any fiscal year (July 1 - June 30) this is equal to 12 times your May 1st monthly salary rate plus your calendar-year-end salary adjustment (Christmas bonus), or the actual base salary paid to you in any fiscal year during which you have less than a full year of service. It does not include overtime, other bonuses and extra compensation.

### Continuous Service

This generally means your uninterrupted service from the date you are hired to the date your employment with the Company is terminated.

Starting July 1, 1976, authorized leaves of absence are not considered a break in service and are counted as continuous service as long as you return to work for the Company immediately after the end of your authorized leave. However, if your leave is more than 12 months, the period in excess of 12 months is not counted.

Break in Service

If you terminate employment and are rehired within 12 months, the time you were away will be counted as continuous service.

However, if you are rehired after one year of absence, you will have a break in service. Your prior continuous service will be counted only if you meet one of the following conditions:

- You had a vested interest in your Deferred Account (see description on pages 5 and 13) when you left, or
- Your prior continuous service is greater than your period of time away from the Company.

Net Profits

This is the amount which is left over after all operating expenses for that year have been paid, including taxes, Christmas bonuses (but not other bonuses), and that year's contribution to the Pension Plan.

## Company Contributions

Each year the Company contributes a portion of the net profits for that fiscal year (July 1 - June 30). The amount of the contribution is determined as follows:

- . 25% of the first $50,000 of net profit, plus
- . 37-1/2% of the next $50,000 of net profit, plus
- . 50% of the net profit in excess of $100,000, plus
- . Any additional amount authorized by the Board of Directors.

The maximum amount which may be contributed is limited by Internal Revenue Service rules. Under present regulations the maximum amount that can be contributed is, because of contributions to the Pension Plan, approximately 10% of the compensation paid to all participants.

## Voluntary Employee Contributions

If you wish to make contributions to the Plan, you may. The Plan provides a sound means of investing some of your money for financial security at retirement or in times of severe financial need.

You may elect to contribute from 2% to 6% of your compensation. The amount you elect will be withheld from your paycheck and deposited in the Trust Fund each month. The minimum contribution is $25.00 a month.

You may change the amount you are contributing, but only one change can be made in any six-month period. You can also choose to stop contributing but, if you do, you cannot start making contributions again for six months.

Starting, stopping and changing contributions is effective on the first of the month. You should file the form designed for these purposes with the Profit Sharing Committee at least 30 days before you want the action to be effective.

### Allocating Your Share

The amount of the Company's contribution which is to be allocated to your account in any year is determined by figuring what percentage your compensation for that year is of the compensation of all participants. That is

| | | | | |
|---|---|---|---|---|
| Your Compensation divided by Compensation of all Participants | x | Total Company Contribution | = | Your Share |

In addition to Company contributions, the gains or losses from investment of the funds are allocated to each participant's account. Amounts which are forfeited by participants who leave the Company before they are fully vested are also allocated among the remaining participants. Forfeitures are held by the fund for one year (see page 14).

## Participants' Accounts

Each participant may have three accounts:

- Deferred Account
- Immediate Vested Account
- Voluntary Account

During your first two years of employment your share of the Company contribution will be put in your Deferred Account. After two years of employment you can elect to take part of the Company contribution in cash (see page 8 Cash Distribution section). If you do not choose to take the cash, the amount you could have taken will be put in your Immediate Vested Account. The balance of your share of the Company contribution for that year will be put in your Deferred Account.

If you make contributions to the Plan, they are put in a separate account, known as your Voluntary Account.

Investment of Accounts

There are three funds in which your share of the Company's contribution may be invested. These are:

Fund A - A "fixed income" fund which consists of money invested in a group annuity contract issued by an insurance company. Each year the insurance company tells us the rate of interest it will guarantee for the coming year.

If you make voluntary contributions to the Plan, they will be invested in Fund A.

Fund B - which consists of assets invested in common and preferred stocks, cash and cash equivalents (e.g., certificates of deposit). Earnings on this fund, as well as growth in the value of investments will vary from year to year depending on market conditions.

Fund L - which consists of assets invested in promissory notes of participants who have borrowed money from the Plan.

Each year (usually in May) you will be given a Selective Investment Form on which you indicate how much of that year's contribution you want invested in Fund A or Fund B, or both. At that time you may also elect to transfer some or all of the current amounts from one Fund to the other. These elections have to be made by May 31st, otherwise your contribution will automatically be put in Fund B. Fund L is only used by participants who borrow some of their money from the Plan to cover the loan. If you apply for a loan from the Plan (see page 9), your office manager or the Accounting Department will explain how this Fund works.

At least once each year you will receive a statement showing the current value of your accounts.

## Payments from the Plan While Actively Employed

During your years of employment with the Company you may have a part of your Profit Sharing accounts paid to you in several different ways, as described in this section. It should be noted that since most of the assets of the Plan are invested in an insurance contract and securities, distribution of funds cannot be made at just any time during the year. Each form of distribution has restrictions on the frequency and time of year it may be made. If you expect to withdraw part of your money, check these restrictions so that adequate notice can be given to the Committee.

The types of payment available are:

- Cash Distribution
- Loans
- Partial Withdrawal prior to age 59-1/2
- Partial Withdrawal after age 59-1/2
- Withdrawal of Voluntary Contributions

Following is a description of each of these payments.

- Cash Distribution - If you have completed two or more years of continuous service on June 30th, you may elect a cash distribution. This payment is made from your share of the Company's contribution to be made for the current year. The amount you may elect to have paid in cash will be the smaller of the amount determined in Columns (2) and (3) of the following table:

| Years of Continuous Service as of June 30th: (1) | Your Share of the Company Contribution Multiplied by: (2) | Your Compensation Multiplied by: (3) |
|---|---|---|
| Less than 2 | 0% | 0% |
| 2 but less than 3 | 20% | 2% |
| 3 but less than 4 | 35% | 3-1/2% |
| 4 and over | 50% | 5% |

Each year in May you will be given a form to indicate the amount of Cash Distribution you want that year. This election must be made by May 31st.

If you do not elect to take the full Cash Distribution to which you are entitled, the balance will be put in your Immediate Vested Account.

- Loans - If you have completed five or more years of continuous service and have not reached age 63, you may borrow money from your accounts for certain specified reasons (e.g., buying a house, college tuition, etc.) with the approval of the Profit Sharing Committee.

Loans may be made quarterly - on July 1, October 1, January 1 and April 1 of each year. You must file a loan application with the Profit Sharing Committee and obtain their approval.

The amount you may borrow will be limited to 50% of the smaller of (a) your compensation, and (b) your Immediate Vested Account plus the vested portion of your Deferred Account.

You must repay the loan, plus interest, in not more than five annual installments (or by the June 30th following your 65th birthday, if earlier). Payments may be made on July 1st each year. The interest rate charged on loans is set by the Profit Sharing Committee, and is currently 7%. If you do not repay the principal of the loan in the time required, the amount still due will be treated as if you had taken a partial withdrawal.

Successive loans are not permitted. Only one loan may be outstanding at a time. A new loan made before full repayment of an old one will be reduced by the amount outstanding and the difference will be paid to you.

. Partial Withdrawals Prior to Age 59-1/2 - You can make a withdrawal of part of your Profit Sharing accounts while you are an active employee, if you have completed seven or more years of continuous service.

The maximum amount you may receive as a partial withdrawal over your career with the Company is the total of:

A. 50% of the Company contributions credited to your Deferred Account, and

B. 100% of the Company contributions credited to your Immediate Vested Account.

The maximum amount you may withdraw in a Plan Year is the smaller of the following:

1. 50% of your compensation on the July 1st on which the distribution would be made, or
2. The remaining career maximum that has not been distributed.

This type of withdrawal is paid in a lump sum, and only once each year, on July 1st. You must file an application with the Committee and obtain their approval.

. Partial Withdrawals After Age 59-1/2 - One partial withdrawal (the maximum permitted by Internal Revenue Regulations) may be made between your attainment of age 59-1/2 and your normal retirement date. You may elect to have this withdrawal paid in a lump sum or in installments over a period of up to 15 years, or used to purchase an annuity. You may withdraw the entire amount of your accounts to which you would [illegible] been entitled if you terminated your employment. Even [illegible] withdraw all of your accounts, you will continue to participate [illegible] Plan as long as your employment continues. You must file an application with the Committee and obtain their approval. Your withdrawal will be paid to you on the first day of any month you choose, but no earlier than the first day of the third month after you apply.

. Withdrawal of Voluntary Contributions - If you have made contributions to the Plan and wish to withdraw this money you may, with the approval of the Committee. Withdrawals can be made only for reasons of financial need, such as illness, education, or other needs related to the welfare of you and your family. You may withdraw all or part of your Voluntary Account, including the earnings on your contributions.

A form for withdrawing must be filed with the Committee. With their approval, your Voluntary Account will be valued as of the end of the month in which they received the request. You will receive the money within 31 days after the Committee notifies the insurance company of the amount to be paid.

If you withdraw any of your Voluntary Account, you must stop making contributions to the Plan for six months. After that, you can start contributing again by notifying the Committee, in writing, at least 30 days before the first day of the month in which you want your contributions to start.

## Payments from the Plan When You are No Longer Employed

You or your beneficiary will be entitled to your Profit Sharing account in the following circumstances.

- Retirement
  Normal Retirement under this Plan is age 62. When you retire, at that age or later, you will be entitled to the full amount of your accounts.

- Disability
  If you become totally and permanently disabled, you will be entitled to the full amount of your accounts.

- Death
  In the event of your death prior to retirement, the full amount of your accounts would be paid to the beneficiary you have designated.

- Termination of Employment
  If you leave the Company for reasons other than normal retirement, disability or death, your accounts will be paid as follows:

  - 100% of your Voluntary Account, plus earnings, plus
  - 100% of your Immediate Vested Account, and
  - the amount of your Deferred Account in which you have a vested interest. This percentage is based on service as shown in the following table:

| Years of Continuous Service | Vested Interest in Deferred Account |
|---|---|
| Less than 3 | 0% |
| 3 but less than 4 | 10% |
| 4 " " " 5 | 25% |
| 5 " " " 6 | 50% |
| 6 " " " 7 | 75% |
| 7 or more | 100% |

Within 31 days after your employment terminates, you must elect to have your Voluntary Account paid immediately, or you may defer payment (with Committee approval as to earnings), until age 62.

If, when you leave the Company, you are not fully vested in your Deferred Account, the amount to which you are not entitled will be held for one year. If you are not rehired during that period, it will then be distributed among the accounts of the present participants. If you are rehired within a year and pay back within 90 days the amount you received when you left, the amount you forfeited when you terminated employment will be returned to your account.

## When Benefits Begin

Benefits will begin after the Committee has received application for payment and on the date selected by the Committee under the terms of the Plan.

## How Plan Benefits are Paid

When a payment is to be made, your account will be valued to reflect the net worth of the funds just prior to distribution to you.

Payments made in the form of a cash distribution, loan, or partial withdrawal before age 59-1/2 will be in a lump sum.

Payment on retirement, disability, death, termination of employment or a partial withdrawal after age 59-1/2 may be made in one of the following ways:

(1) A Lump sum

(2) Installments over a period of up to 15 years

(3) Purchase of an annuity contract.

You may elect the method of payment you prefer, subject to approval by the Committee. If you have not made an election and you are married when a payment is due, the automatic form will be a Joint and Survivor Annuity. This will provide a monthly income to you during your lifetime and after your death, 50% of that amount would be paid to your spouse for his or her remaining lifetime. If you do not want this form of payment, you should make your election in writing and file it with the Committee before a payment is due.

Several forms of annuities may be elected, including a Variable Annuity, which provides a monthly income which changes to reflect current market conditions. A Variable Annuity is only available at retirement and if you have money in Fund B.

If payments are to be made in installments or under an annuity, the period of time over which payments are to be made cannot exceed your life expectancy (and that of your spouse if he or she is to receive benefits).

## Taxes on Benefits

You do not have to pay taxes on your benefits until you actually receive them. When payment is made, Company contributions and all earnings will be subject to tax. The amount of tax you will have to pay will depend on the type of distribution, your status at the time and the tax laws in effect when the payment is made. Before you apply for distribution of your accounts you should consult with a tax advisor about the consequences of the various types of payment.

## How to Apply for Benefits

All benefits from the Plan must be applied for, in writing, and approved by the Committee. The necessary forms for the type of payment you want made may be obtained from your office manager or the Accounting Department. All applications require time for Committee consideration, valuation and adjustment of your account and, in some cases, notification to the insurance company. Therefore, you should file your application as far in advance as possible of the date you want payment made.

## Appealing a Denied Claim

If you make a claim for benefits under the Plan, and all or part of it is denied, the Profit Sharing Committee will notify you of their action and reasons with specific reference to the Plan provisions which they feel apply. They will also tell you how you can appeal their decision. The appeal process is stated below for your information.

1. Within 60 days of receiving the Committee's determination letter, you may send a certified or registered letter to the Secretary, Profit Sharing Committee, c/o Accounting Department, The Wyatt Company, 1050 Seventeenth Street, N. W., Washington, D. C. 20036, indicating your reasons for appeal and any additional information to support your claim for benefits.

2. If the Profit Sharing Committee, after reviewing this information, still determines you are not entitled to the benefits you claim, they will give you or your representative an opportunity to appeal by either (i) appearing personally before the Chairman of the Committee to give further written or oral support to your claim and to review any pertinent documents, or (ii) making written appeal to the Chairman of the Committee in which you may also request copies of pertinent documents.

3. Within 60 days of your appeal (or 120 days in complex situations), whether by personal appearance or written,the Committee Chairman will notify you by certified letter of the final decision and the specific reasons for the decision.

4. You may also direct your appeal to the President of the Company if you desire.

## Administration of the Plan

The Profit Sharing Plan is a Defined Contribution Plan. The Wyatt Company is the administrator of the Profit Sharing Plan and acts as the Plan Fiduciary. The Profit Sharing Committee is appointed by the Board of Directors of the Company to carry out the administration of the Plan. The Committee is made up of at least three Wyatt associates, who receive no pay for this work.

The Committee makes all the rules and regulations necessary to administer the Plan efficiently. Although they cannot alter the terms, conditions or benefits of the Plan, they make all decisions regarding any question, interpretation or application of any Plan provisions. The Committee also reviews all applications for loans, withdrawals, distributions, investments and other benefits by Plan members to ensure that all Plan provisions are put into practice uniformly and without discrimination.

The cost of administering the Plan is paid for by the Company.

## Other Important Information

### Prior Plan Provisions

Under the Plan prior to the July 1, 1976 amendment, participants were allowed to contribute up to 10% of their earnings. Because of ERISA the maximum contribution rate is now 6%. If you were contributing more than that you may continue to as long as you do not withdraw or suspend your contributions. If you do and subsequently wish to contribute again, the maximum rate of 6% will apply. If you want to change to a lower rate, (e.g., 9%) you may, but you cannot subsequently change it back to the higher rate.

### Continuance of the Plan

The Company fully intends to continue the Profit Sharing Plan indefinitely and to meet any foreseeable situations that may occur. To protect against any unforeseen situations, the Company does reserve the right to change the Plan and, if absolutely necessary, discontinue it. If it is necessary to discontinue the Plan, the assets of the Plan less any necessary final expenses will be used to provide benefits for Plan participants as if all were eligible for retirement at the close of that fiscal year. You should also understand that this is not the type of plan that is insured by the Pension Benefit Guaranty Corporation and therefore, is not covered by its plan termination insurance provisions.

### Plan Document

This booklet is a summary of the provisions of the Profit Sharing Plan Document. We have tried to write this summary in clear, understandable and informal language. Please refer to the official Plan Document for more extensive information. In the event of any conflict between this booklet and the Plan Document, the Plan Document will govern.

You are entitled to examine the Plan Document, the Plan Description (Form EBS-1) and the Plan Annual Report as soon as they are filed with the Secretary of Labor. Your office manager has a copy of these documents that you may see during working hours. If you would rather have a copy of these documents, send a written request to the Accounting Department, The Wyatt Company, 1050 Seventeenth Street, N. W., Washington, D. C. 20036.

### Summary Annual Report and Plan Changes

You will receive a summary of the annual report of the Plan once each year at no charge. As modifications to the Plan are made, you will also be notified.

### Assignment of Benefits

For the protection of your interests and those of your dependents, your benefits under this Plan cannot be assigned and, to the extent permitted by law, are not subject to garnishment or attachment.

### Agent for Service of Legal Process

The Wyatt Company, 1050 Seventeenth Street, N. W., Washington, D. C. 20036. Service may also be made on the Trustees or the Committee.

### Profit Sharing Committee

For your information, the four members of the Profit Sharing Committee currently are:

Edward M. O'Rourke, Chairman
Consultant, The Wyatt Company
Suite 5600 Sears Tower
233 South Wacker Drive
Chicago, Illinois 60606

J. Perham Stanley
Vice President and Treasurer
The Wyatt Company
200 First National Building
Detroit, Michigan 48226

Herbert W. Osterman
Actuary, The Wyatt Company
90 Park Avenue
New York, New York 10016

Frederick S. Little
Controller, The Wyatt Company
1050 Seventeenth Street, N. W.
Washington, D. C. 20036

Your questions and comments on the Profit Sharing Plan may be addressed to these individuals for assistance.

The Trustees are:

Fund A:
Mutual Life Insurance Company of New York
New York, New York 10019
(212) 586-4000

Fund B:
National Bank of Detroit
Woodward & Fort
Detroit, Michigan 48232
(313) 225-1000

### Fiscal Year

The Fiscal Year begins on July 1 and ends June 30th. This is the same as the Plan Year.

Employer Identification Number - 53-0181291

Plan Number - 002

## Your Rights under the Employee Retirement Income Security Act of 1974

As a participant in The Wyatt Company Profit Sharing Plan you are entitled to certain rights and protections under the Employee Retirement Income Security Act of 1974 (ERISA). ERISA provides that all plan participants shall be entitled to:

- Examine, without charge, at the plan administrator's office and at other specified locations, all plan documents, including insurance contracts, and copies of all documents filed by the Plan with the U.S. Department of Labor, such as detailed annual reports and plan descriptions.

- Obtain copies of all plan documents and other plan information upon written request to the plan administrator. The administrator may make a reasonable charge for the copies.

- Receive a summary of the Plan's annual financial report. The plan administrator is required by law to furnish each participant with a copy of this summary annual report.

- Obtain a statement telling you whether you have a right to receive a benefit at normal retirement age (age 62) and if so, what your benefits would be if you stop working under the Plan now. If you do not have a right to a benefit, the statement will tell you how many more years you have to work to get a right to a benefit. This statement must be requested in writing and is not required to be given more than once a year. The Plan must provide the statement free of charge.

In addition to creating rights for Plan participants, ERISA imposes duties upon the people who are responsible for the operation of the employee benefit plan. The people who operate your Plan, called "fiduciaries" of the Plan, have a duty to do so prudently and in the interest of you and other Plan participants and beneficiaries.

No one, including your employer, or any other person, may fire you or otherwise discriminate against you in any way to prevent you from obtaining a benefit from this Plan or exercising your rights under ERISA.

If your claim for a benefit is denied in whole or in part you must receive a written explanation of the reason for the denial. You have the right to have the plan administrator review and reconsider your claim.

Under ERISA, there are steps you can take to enforce the above rights. For instance, if you request materials from the Plan and do not receive them within 30 days, you may file suit in a federal court. In such a case, the court may require the plan administrator to provide the materials and pay you up to $100 a day until you receive the materials, unless the materials were not sent because of reasons beyond the control of the administrator. If you have a claim for benefits which is denied or ignored, in whole or in part, you may file suit in a state or federal court. If it should happen that plan fiduciaries misuse the Plan's money, or if you are discriminated against for asserting your rights, you may seek assistance from the U.S. Department of Labor, or you may file suit in a federal court.

The court will decide who should pay court costs and legal fees. If you are successful the court may order the person you have sued to pay these costs and fees. If you lose, the court may order you to pay these costs and fees, for example, if it finds your claim is frivolous.

If you have any questions about your Plan, you should contact the plan administrator. If you have any questions about this statement or about your rights under ERISA, you should contact the nearest Area Office of the U.S. Labor-Management Services Administration, Department of Labor.

Chairman **Pickle**. As I said from the very beginning, we are not attempting to advance this legislation with the intent of passing it this week or next week. Very likely it will be something we will keep on the books, and hope that we might be able to make it part of some legislation pending in the next session. We may hold hearings again about this next year.

But most of these items are changes that, though we have had two or three questions raised, by and large they are things that long since have either become the law, or are actually being practiced administratively by the SSA now. That was the purpose and the intent of the entire bill. We don't want to be trying to push something here that is going to be extremely controversial or objectionable.

I do know in cases like yours, Ms. Sweeney, that we will be awaiting the decision of the *Edwards* case. It would be a little difficult to try to outguess the courts anymore than we tried to outguess Treasury on how much the interfund borrowing group will actually borrow at the end of this month. But we will be watching and will be mindful of any court action. And we will visit with you and others as we go along with this.

We wanted to get this testimony on the record today for study by the committee and perhaps for further hearings or study later. So I appreciate you people coming and testifying. It was short notice. We know that. We had hoped that we might have been able to have done this earlier, but a lot of things have held us up.

But at least we wanted people to know what they were thinking of. There is a possibility that one or two other items will be added to this bill. No testimony was taken on them today, but some of the members of the committee raised the possibility of putting something in the bill with respect to illegal aliens, or aliens that reside in the country, not illegal aliens. I don't know about this, but it might be a possibility which might be controversial. We are not trying to push that in this bill, but rather to let everybody know what our general intentions are and to receive testimony from any other groups who want to submit it.

Ms. **SWEENEY**. Mr. Pickle, in that regard, short notice, I have been asked by many of the groups representing women's organizations to tell you that they will be submitting statements. There are a couple provisions, in addition to the Edwards one, they are concerned about where there is an equalizing down instead of equalizing up. I believe they will be submitting it for the record by the 17th.

Chairman **PICKLE**. That will be fine.

I thank you and all the witnesses who appeared before us this afternoon. Your testimony has been very helpful.

The subcommittee will stand adjourned.

[Whereupon, at 4:20 p.m., the hearing was adjourned.]

[Submissions for the record follow:]

## STATEMENT OF HON. JOHN F. SEIBERLING, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF OHIO

Mr. Chairman and Members of the Subcommittee, I appreciate the opportunity to present my views on proposed technical and minor changes in Title II of the Social Security Act.

Mr. Chairman, since our constituents have to live with the laws we pass, we frequently hear from them about changes they think are necessary. I recently received a letter from a constituent concerning social security taxes paid on services performed by baby sitters. He believes that the existing $50-per-quarter exemption, established in the 1950's, is now too low, and that he and many others who hire babysitters must comply with payroll tax withholding procedures intended to apply to domestic employees who work many more hours.

I agree that the $50-a-quarter ceiling for babysitters should be increased, and have introduced legislation for that purpose. A copy of the bill is attached. While I recognize that this problem is insignificant in relation to the difficult issues that this subcommittee will grapple with in the near future, I hope that you will have an opportunity to include such an improvement in the final title of next year's social security financing legislation.

Thank you very much.

## H.R. —

A bill to amend title II of the Social Security Act and the Internal Revenue Code of 1954 to exclude from wages, for purposes of computing benefits and taxes under the old-age, survivors, and disability insurance program, the quarterly cash remuneration for the services of a domestic employee in a private home of the employer if such quarterly cash remuneration is less than $200 or the employee has not attained age 19 before the beginning of the quarter.

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,* That (a) section 209(g)(2) of the Social Security Act is amended by striking out "if the cash remuneration paid in such quarter by the employer to the employee for such service is less than $50." and all that follows and inserting in lieu thereof "if the cash remuneration paid in such quarter by the employer to the employee for such service is less than $200 or the employee has not attained age 19 before the beginning of such quarter. Nothing in subsection (h)(2) shall be construed to limit the effect of this paragraph;".

(b) Section 3121(a)(7)(B) of the Internal Revenue Code of 1954 is amended by striking out "if the cash remuneration paid in such quarter by the employer to the employee for such service is less than $50." and all that follows and inserting in lieu thereof "if the cash remuneration paid in such quarter by the employer to the employee for such service is less than $200 or the employee has not attained age 19 before the beginning of such quarter. Nothing in paragraph (8)(B) shall be construed to limit the effect of this subparagraph;".

SEC. 2. The amendments made by the first section of this Act shall apply with respect to calendar quarters beginning on or after January 1, 1983.

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CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA,
*Washington, D.C., December 16, 1982.*

Hon. J. J. PICKLE,
*Chairman, Subcommittee on Social Security, Committee on Ways and Means, House of Representatives, Washington, D.C.*

DEAR MR. CHAIRMAN: On behalf of the U.S. Chamber's over 244,000 members, I offer the following comments on H.R. 7326, The Social Security Miscellaneous and Technical Improvements Act of 1982.

Since the financial problems besetting Social Security became evident in the mid-70's, the Chamber has consistently advocated four steps: slow the future growth of benefit entitlement; rid the program of the administrative shortcomings that waste precious program resources; broaden the tax paying base by mandating universal coverage; and maintain payroll tax financing of the program. Most of the provisions of H.R. 7326 are consistent with this position in that they would greatly aid in the efficient administration of the Social Security program. We, therefore, support those provisions.

The cash management provisions under Title I fall into this category. The four sections of that title would correct certain program administrative shortcomings which are unnecessarily depleting the program of much needed reserves. We strongly support passage of all the provisions under this Title.

On a less positive note, there is one section of H.R. 7326 that we would urge the Subcommittee to examine closely—that is, Section 304. This provision would amend the Internal Revenue Code and the Social Security Act to include elective payments to a profit sharing or stock bonus plan described under Section 401(k) of the Code in the definition of wages for the purpose of subjecting them to the FICA tax. We see administrative as well as equity and policy difficulties with this proposed change.

Administratively, Section 304 would require a significant increase in the already excessive recordkeeping burden upon employers. This has grave implications for smaller employers. By requiring that the Social Security tax be applied to profit sharing contributions, this provision would require employers to maintain separate gross income amounts for FICA taxes as opposed to federal, state, city income as well as FUTA taxes. The difficulty of this change is compounded by the fact that the income in question is not currently processed through the normal payroll system. In addition to this recordkeeping problem would be the cost and difficulties of the necessary modifications to payroll procedures, computer systems, paycheck stubs, reporting forms, and the cost of the explanation and communication to employees effected by the change.

Moreover, we must question the equity and policy question that arises from changing 401(k) plans, a pension arrangement of particular interest to small employers because of its simplicity and administrative ease. The financial difficulties of Social Security should suggest to us the need for additional incentives for employers and employees to work together to lessen retirement dependence upon Social Security. On that score, Congress should be moving in the exact opposite direction of Section 304.

The current procedure of not subjecting deferred income contributions under an approved 401(k) plan to any type of taxation, until that contribution is received in the form of income, is a valuable incentive for individuals to save for their own retirement. To compromise this incentive solely for the short-term prospect of slight amounts of additional revenues for the Social Security program would be a mistake. The fact that the individual's benefit check may also be slightly lower is not a fault in the current system. The individual, in the long-run, has a more well rounded and probably more lucrative retirement package. That is good for the individual, good for Social Security and, therefore, good for the Nation.

Other areas of H.R. 7326, specifically Sections 301, 302, 303 and 305, are also of interest to the business community. We are currently studying those provisions and will reserve comment upon them until a later date.

We appreciate the leadership the Subcommittee has continued to show by addressing the many miscellaneous and technical items covered by H.R. 7326 and request that this statement be made a part of the hearing record.

Cordially,

HILTON DAVIS,
*Vice President,*
*Legislative and Political Affairs.*

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## STATEMENT OF NANCY DUFF CAMPBELL, ON BEHALF OF THE AMERICAN ASSOCIATION OF UNIVERSITY WOMEN, AMERICAN NURSES ASSOCIATION, NATIONAL COMMISSION ON WORKING WOMEN, NATIONAL COUNCIL OF CATHOLIC WOMEN, NATIONAL COUNCIL OF JEWISH WOMEN, NATIONAL FEDERATION OF BUSINESS AND PROFESSIONAL WOMEN'S CLUBS, INC., NATIONAL WOMEN'S HEALTH NETWORK, NATIONAL WOMEN'S LAW CENTER, OLDER WOMEN'S LEAGUE, UNITARIAN UNIVERSALIST WOMEN'S FEDERATION, WOMEN'S EQUITY ACTION LEAGUE, AND WOMEN'S LEGAL DEFENSE FUND

### SUMMARY

1. This statement was prepared by Nancy Duff Campbell, an attorney with the National Women's Law Center, on behalf of the American Association of University Women, American Nurses Association, National Commission on Working Women, National Council of Catholic Women, National Council of Jewish Women, National Federation of Business and Professional Women's Clubs, Inc., National Women's Health Network, National Women's Law Center, Older Women's League, Unitarian Universalist Women's Federation, Women's Equity Action League, and Women's Legal Defense Fund.

2. The American Association of University Women, American Nurses Association, National Commission on Working Women, National Council of Catholic Women, National Council of Jewish Women, National Federation of Business and professional Women's Clubs, Inc., National Women's Health Network, National Women's Law Center, Older Women's League, Women's Equity Action League, and Women's Legal Defense Fund are national organizations working to secure the legal and economic rights of women in American society. In particular, we are concerned about discrimination in Title II of the Social Security Act because of the large numbers of women and their families who are beneficiaries of the Social Security system.

3. We are pleased with the bill's effort to correct the remaining provisions of Title II of the Social Security Act which, on their face, discriminate on the basis of gender. However, we are concerned about the solutions to gender discrimination that the bill proposes in Sections 205, 207, 208 and 209, and propose alternative solutions for these sections that we hope the Subcommittee will adopt.

4. In Sections 205, 207 and 208, the gender discrimination in current provisions of the Social Security Act has been eliminated by an "equalizing down" rather than an "equalizing up" of benefits, which will result in a loss of benefits for individuals who would otherwise be eligible. We propose, for the reasons set out more fully in the attached statement, that the discrimination be eliminated by an "equalizing up" of benefits.

5. In Section 209, which adddresses the treatment of income from self-employment in community property states, the bill's provision that the earnings from such income be credited to the spouse who exercised the greater management and control over the trade or business is not an equitable solution and is inconsistent with the solution arrived at by the courts, most particularly with the decision in a nationwide class action brought on behalf of women injured by the current provision, *Edwards* v. *Schweiker,* No. C-80-3958 (N.D. Cal. Jan. 22, 1982), *appeal dismissed,* No. —— (9th Cir. Aug. 12, 1982), *petition for cert. filed,* No. —— (O.T. 1982, Nov. 24, 1982). In our view the solution ordered by the *Edwards* court, which requires the Secretary to evaluate the division of labor between the couple and allocate earnings accordingly, is the appropriate solution to the gender discrimination in the current provision. In addition, the *Edwards* court's determination to apply its decision retroactively to all years in which individuals injured by the provision were affected is essential to eliminating the gender discrimination in the current provision and should therefore be a part of any bill to correct that discrimination. Because the solution to discrimination that we advocate involves more than technical changes in the current provision, and the *Edwards* case is on appeal to the Supreme Court, we recommend that Section 209 be deleted and the question of the appropriate legislative solution to the problem addressed by Section 209 be deferred at this time.

6. We understand that Senator Dole, in reintroducing in the 98th Congress his bill to similarly correct the remaining provisions of the Social Security Act that, on their face, discriminate on the basis of gender, has agreed to the changes we are proposing in sections 205, 207 and 208, and to the deletion of Section 209.

This statement presents the views of the American Association of University Women, American Nurses Association, National Commission on Working Women, National Council of Catholic Women, National Council of Jewish Women, National Federation of Business and Professional Women's Clubs, Inc., National Women's Health Network, National Women's Law Center, Older Women's League, Women's Equity Action League, and Women's Legal Defense Fund on the provisions of Title II of H.R. 7326, the Social Security Miscellaneous and Technical Amendments Act of 1982. Because these provisions address explicit gender discrimination in the Social Security Act, they are of concern to our organizations which are working to secure the legal and economic rights of women in American society.

We are pleased with the bill's effort to correct the remaining provisions of Title II of the Social Security Act which, on their face, discriminate on the basis of gender. However, we are concerned about the solutions to gender discrimination that the bill proposes in Sections 205, 207, 208 and 209. In Sections 205, 207 and 208, the discrimination has been eliminated by an "equalizing down" rather than an "equalizing up" of benefits, which will result in a loss of benefits for individuals who would otherwise be eligible under current law. In Section 209, which addresses the treatment of self-employment income in community property states, the bill's provision that the earnings from such income be credited to the spouse who exercised the greater management and control over the trade or business is not an equitable solution and is inconsistent with the solution arrived at the courts. Each of our concerns is described in more detail below; we propose alternatives to the bill's solutions in Sections 205, 207, and 208, and propose that Section 209 be dropped from the bill and from legislative consideration at this time.

Before discussing these provisions in detail, we would like to call the Subcommittee's attention to S. 3008, a bill that would, in Title II, similarly correct the remaining provisions of the Social Security Act that, on their face, discriminate on the basis of gender. In its original draft form, Title II of S. 3008 was essentially the same as H.R. 7326. However, after several of our organizations met with members of Senator Dole's staff to express our concerns about the same provisions that we are concerned about in H.R. 7326, Senator Dole agreed to delete those provisions from S. 3008, and worked with us further on solutions to the problems that the provisions were intended to address. It is now our understanding that S. 3008 will be redrafted to incorporate all of the changes we propose here before it is reintroduced in the 98th Congress. We hope that the Subcommittee, too, will accept these changes, so that the two bills can be brought into conformity and move forward quickly to final passage by both houses of Congress.

Section 205 amends the current provision of the Social Security Act that provides benefits to certain uninsured individuals who attained age 72 prior to 1968. See 42 U.S.C. § 428. Under the current provision, once a husband and wife are separately determined to be eligible for benefits, the couple is treated as if the husband were the retired worker and the wife were the dependent. As a result, their payment, which is provided largely from general revenues, is allocated so that the husband is paid two-thirds of it and the wife is paid one-third. Section 205 of the bill changes this is require that the payment be divided equally between them.

The problem with the solution proposed by Section 205 is that it results in a reduction of benefits to husbands in such situations. In our view, the solution should be to "equalize up" rather than "equalize down," and to provide both spouses with the full benefit they would be entitled to if they were not married. The rationale for this approach is that this is a special benefit that is not based on either spouse's status as a retired worker or as a dependent and hence the couple should in no sense be treated as if they were worker and dependent, as Section 205 does. Moreover, this is a benefit that affects very few people and is small in amount; therefore the cost of providing it in its full amount to both spouses is small.

Sections 207 and 208 address the effect of marriage on the benefits of certain recipients. Under current provisions of the Social Security Act, when an individual receiving benefits as a dependent child of a disabled, retired or deceased worker marries, the individual's benefits terminate because the law presumes that the dependency situation no longer exists. An exception is made when one Social Security beneficiary marries another, because it cannot be presumed that either one is able to support the other. Thus, in general, when a childhood disability beneficiary marries another Social Security beneficiary, neither spouse loses benefits because of the marriage. However, when a childhood disability beneficiary marries another childhood disability beneficiary or a disabled worker beneficiary, and subsequently one of the beneficiaries recovers or engages in substantial work, the continued eligibility of the spouse depends upon the spouse's gender. A women's childhood disability benefits end when her husband's disability benefits end. In contrast a man's childhood disability benefits do not end when his wife's disability benefits end. The rationale is that men who are no longer disabled are expected to support their wives, but women who are no longer disabled are not expected to support their husbands. See 42 U.S.C. § 402(d).

Similarly, in general, when a childhood disability beneficiary or disabled worker beneficiary marries a beneficiary of certain kinds of Social Security benefits, and the disabled beneficiary recovers or engages in substantial work, the continued eligibility of that individual's spouse depends upon the gender of the individual. If the disabled individual is a man, and his benefits end, his wife's benefits also end. If, however, the disabled individual is a woman, her husband's benefits do not end when her benefits end. The rationale is the same as above: no-longer-disabled men are expected to support their wives; no-longer-disabled women are not expected to support their husbands. See 42 U.S.C. § 402(d).

Section 207 of H.R. 7326 corrects the gender discrimination in the first situation by terminating the benefits of childhood disability beneficiaries, regardless of gender, when the beneficiary's spouse is no longer eligible for benefits. Section 208 corrects the gender discrimination in the second situation by terminating the benefits of individuals receiving dependents' or survivors' benefits, regardless of gender, when the individual's spouse is no longer eligible for benefits. In both these situations, the bill "equalizes down" rather than "equalizes up," which results in a loss of benefits to certain individuals who would otherwise have been eligible for such benefits. (The bill has a future effective date and therefore would not affect current beneficiaries.) In our view, in neither situation should a loss of benefits occur, because individuals entitled to Social Security benefits who marry individuals who are entitled to disability benefits should not lose their entitlement to such benefits merely because their spouse has lost his or her eligibility for benefits. Their benefits are not benefits they receive as dependents or survivors of their spouses and should not be tied to their spouses' benefits. Moreover, to the extent that both the current law provisions and the changes effectuated by Sections 207 and 208 are based on a presumption that "recovered" disability beneficiaries are able to support their spouses fully, they fail to take account of the extent to which "recovery" may be a slow process, may never result in full employment for the "recovered" individual and may, indeed, eventually end because of a recurrence of the disability or related conditions. In none of these circumstances is the "recovered" individual likely to be able to provide fully for his or her spouse, not to mention other members of the family who, with the loss of the spouse's Social Security benefits, may be totally dependent upon the "recovered" individual for their livelihood as well. Finally because the number of disability beneficiaries (particularly childhood disability beneficiaries) who marry other Social Security beneficiaries and thereafter recover from their disabilities or engage in substantial work is small, the cost of "equalizing up" rather than "equalizing down" is small.

Section 209 addresses the treatment of self-employment income in community property states. Under the current provision of the Social Security Act, all income earned by a husband and wife operating a trade or business is, in community property states,[1] credited to the husband unless the wife can establish that she exercised "substantially all of the management and control of such trade of business." 42. U.S.C. § 411(a)(5)(A). This provision has been declared unconstitutional on the grounds of gender discrimination by several courts, most significantly in a nationwide class action brought on behalf of all women injured by the provision, *Edwards* v. *Schweiker*, No. C-80-3959-MHP (N.D. Cal. Jan. 22, 1982), *appeal dismissed*, No. —— (9th Cir. Aug. 12, 1982), *petition for cert. filed*, No. —— (O.T. 1982, Nov. 24, 1982).[2] *See also Hester* v. *Harris*, 631 F.2d 53 (5th Cir. 1980); *Carrasco* v. *Secretary of Health, Education & Welfare*, 628 F.2d 624 (1st Cir. 1980); *Becker v. Harris*, 493 F. Supp. 991 (E.D. Cal. 1980). The solution to the unconstitutional gender discrimination ordered by the *Edwards* court,[3] however is very different from that proposed by

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[1] The jurisdictions that are currently community property jurisdictions are Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Puerto Rico, Texas and Washington.

[2] We understand that a copy of the decision in *Edwards* has been made available to the Subcommittee as an attachment to the testimony of Eileen P. Sweeney, and therefore we have not attached a copy of the decision to this statement.

[3] *Hester*, *Carrasco* and *Becker* are not class actions; hence, the focus of the discussion here will be on the nationwide relief ordered in *Edwards*.

Section 209 of H.R. 7326, and more equitable. Under the *Edwards* decision, the Secretary is required to allocate income from a coproprietorship between the spouses according to the "relative amounts of labor contributed by each" to the earning of that income. In contrast, under Section 209 of H.R. 7326, unless a partnership exists, all of the earnings will be credited to the spouse who exercised the greater management and control over the trade or business. No division of earnings is permitted, despite the fact that both spouses worked to accumulate those earnings. The *Edwards* court expressly rejected this standard as inequitable, and as inconsistent with case law on the treatment of income from a co-proprietorship in non-community property states.[4] The Subcommittee, too, should reject this standard.

The effective date of October 1980 contained in Section 209 is also inconsistent with the relief ordered by the *Edwards* court, which provides that individuals harmed by the unconstitutional gender discrimination are entitled to a recomputation of their earning records, "extending back to the beginning of Social Security, if necessary." Here, too, the flaw in the bill's approach is important because, unlike most changes that affect benefits and for which imposition of an arbitrary effective date may be appropriate, the result of applying an effective date of October 1980 to the recalculation of earnings is to perpetuate the unconstitutional discrimination for many years to come, since only earnings (and earning credits) accumulated after that date will be counted.

Because the changes we would like to see made in Section 209 are more than technical changes, and the *Edwards* case is currently on appeal to the Supreme Court, we recommend that Section 209 be deleted from the bill and the question of the appropriate solution to the problem addressed by Section 209 be deferred until the *Edwards* litigation has run its full course. At some point in the future, either after *Edwards* has been fully implemented or when the Subcommittee is considering a bill containing more controversial provisions than those in H.R. 7326, this issue can be addressed.

In sum, we recommend that Sections 205, 207 and 208 be changed to provide for an "equalizing up" rather than an "equalizing down" of benefits, and that Section 209 be deleted from the bill.

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## STATEMENT OF PFIZER, INC.

We at Pfizer strongly support Section 304 of the Social Security Technical Improvement Act, H.R. 7326, introduced on November 30, 1982 by Representative J. J. Pickle, the Chairman of the House Social Security Subcommittee. We believe the change contained in Section 304 is in the best interest of the government, individuals affected, and the private sector.

Section 304 would include as "wages" for social security tax and benefit purpose certain amounts that an employee elects to have deferred under a plan described in Section 401(k) of the Internal Revenue Code. Section 401(k) encourages saving for retirement by permitting employees to save by deferring income. Section 401(k) encourages employers to obtain the broadest participation possible on the part of employees.

The change proposed by Section 304 will remove an aspect of the 401(k) deferral arrangement that we feel unjustly penalizes employees earning below the social security annual taxable wage base, which will be $35,700 in 1983, and discourages such individuals from participating in 401(k) plans. Specifically, social security benefits will be reduced for employees whose total annual income is below the annual taxable wage base or whose social security earnings are lowered below that base as a result of the deferrals. Moreover, the government is deprived of the revenue the social security trust fund otherwise would have received. It is noteworthy that in the case of similar type deferral arrangements (i.e., set asides by employees for 403(b) annuities and Individual Retirement Accounts) no exclusion for such amounts from the FICA tax wage base is provided.

Pfizer is implementing a 401(k) plan in 1983 and we have received expressions of concern from employees whose social security benefits would be reduced by reason of contributing to the plan. Present law furnishes a disincentive for employees in that situation to save. The proposed change would remedy this problem.

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[4] See, e.g., *Rasmussen* v. *Gardner*, 374 F.2d 589 (10th Cir. 1967); *Delno* v. *Celebrezze*, 347 F.2d 159 (9th Cir. 1956); *Raines* v. *Harris*, 508 F. Supp. 17 (W.D. Va. 1980); *Frieburg* v. *Mathews*, CCH Unempl. Ins. Rptr. ¶15,226 (S.D. Ill. 1977); *Dickman* v. *Finch*, 315 F. Supp. 1071 (E.D. Wis. 1969). These cases are discussed in more detail in the testimony before the Subcommittee of Eileen P. Sweeney.

In short, Pfizer, Inc. vigorously supports Section 304 of the Social Security Technical Improvement Act as a provision that will raise needed revenue for the social security system, will encourage saving for retirement by all our employees through greater participation in our 401(k) plan, and will prevent an unjust reduction in the social security benefits of a large number of our employees participating in the 401(k) plan.

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WESTINGHOUSE ELECTRIC CORP.,
*Pittsburgh, Pa., December 8, 1982.*

Hon. J. J. PICKLE,
*Chairman, Subcommittee on Social Security, Committee on Ways and Means, Longworth House Office Building, Washington, D.C.*

DEAR MR. CHAIRMAN: This letter is submitted in connection with the Social Security Subcommittee's December 6 hearing on H.R. 7326, the "Social Security Miscellaneous and Technical Improvements Act of 1982," and is intended for inclusion in the printed record of the hearing.

On behalf of Westinghouse Electric Corporation, I am writing to express strong support for Section 301 of H.R. 7326, which would expand the availability of the election for social security and private pension coverage of U.S. citizens employed by foreign affiliates of American employers. Section 301 would permit the election to be made with respect to foreign affiliates in which the American employer holds a direct or indirect ownership interest of at least 10 percent. This provision is a highly desirable and long overdue correction of present law.

Due to existing restrictions on the availability of the election, for a number of years Westinghouse has been unable to provide social security coverage (and coverage under Westinghouse benefit plans linked to social security coverage) to a growing number of its employees who have been transferred to the payrolls of certain of its foreign subsidiaries. The restrictions of present law have this effect primarily for two reasons. First, it has become increasingly common for Westinghouse to enter into joint ventures at the second-tier level in foreign countries where local law requires a majority local ownership. In addition, it is often necessary for Westinghouse to engage in business in foreign countries at the third-tier level. These factors should not constitute an impediment to the election of social security and private pension coverage for the employees working overseas.

Section 301 of H.R. 7326 would enable Westinghouse to provide social security and private pension coverage for most U.S. citizens that it employs abroad, and we urge that this provision be enacted as soon as possible. However, we do suggest that the bill be clarified in one respect. It is our understanding that Section 301 is intended to extend coverage to foreign subsidiaries below the second-tier level, and we suggest that this intention be more clearly expressed in the bill. This could be achieved by adding the words "directly or indirectly" at the beginning of line 23 of page 38 of the bill. Enclosed is a copy of page 38 with this addition marked.

Again, we express our strong support for Section 301 of H.R. 7326, and we commend the Subcommittee for directing its attention to this matter.

Sincerely,

A. W. FRISCH,
*Vice President and General Tax Counsel.*

Enclosure.

(II) in paragraph (1), by striking out "any other corporation" and inserting in lieu thereof "any other trade or business".

(b)(1) Section 210(a) of the Social Security Act (as amended by subsection (a)(1) of this section) is further amended by striking out "subsidiary" wherever it appears in the matter preceding paragraph (1) and inserting in lieu thereof "affiliate".

(2)(A) Section 3121(l)(8) of the Internal Revenue Code of 1954 is amended—

(i) in the heading, by striking out "SUBSIDIARY" and inserting in lieu thereof "AFFILIATE";

(ii) in the matter preceding subparagraph (A), by striking out "subsidiary" and inserting in lieu thereof "affiliate";

(iii) in subparagraph (A), by striking out "corporation not less than 20 percent of the voting stock" and inserting in lieu thereof "trade or business not less than 10 percent"; and

(iv) by amending subparagraph (B) to read as follows:

"(B) a foreign trade or business that is directly or indirectly owned by or related to a foreign trade or business described in subparagraph (A), if the percentage of that ownership or relationship, when multiplied * * *."

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